92-1719

Nos. ——

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

ESTATE OF JOHN L. BOHN, *et al.*,
Petitioners,

v.

PAUL WADDELL, *et al.*,
Respondents.

ARTHUR J. ABBOTT, *et al.*,
Petitioners,

v.

PAUL WADDELL, *et al.*,
Respondents.

Petition for Writ of Certiorari to the Court of Appeals of the State of Arizona, Division One

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

The question presented for review is:

> Whether a state violates the Due Process Clause when, under legal compulsion, it collects unconstitutional taxes from its citizens, provides its citizens a clear and certain remedy to recover the unlawful exaction, and then, after collecting the taxes, eliminates any clear and certain remedy?

PARTIES TO THE PROCEEDING

Petitioners are the Estate of John L. Bohn, Shirley Bohn, Donald and Mary Rutan, Carl Linton, Arthur Abbott, 4,823 other individually-named petitioners who are retired federal employees, their estates or personal representatives,* and, under the doctrine of virtual representation, the class of approximately 65,000 other retired federal employees, their estates and personal representatives. The respondents are Paul Waddell, the Director of the Arizona Department of Revenue, Craig Cormier, the Assistant Director of the Arizona Department of Revenue, and the Arizona Department of Revenue.

* A list of the individual Petitioners is attached as Appendix I.

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PETITION FOR WRIT OF CERTIORARI

Petitioners, Estate of John L. Bohn, Shirley Bohn, Donald and Mary Rutan, Carl Linton, Arthur Abbott, and the individually-named petitioners listed in Appendix I, on behalf of themselves and all others similarly situated, respectfully petition this Court for a writ of certiorari to the Court of Appeals of the State of Arizona, Division One.

OPINIONS BELOW

Of the two opinions of the Arizona Court of Appeals, the opinion in *Estate of Bohn* is as yet unreported (App. A at 1a) and the opinion in *Abbott* is a memorandum opinion which will not be published (App. B at 26a). The decisions of the Arizona Supreme Court denying Petitioners' Petitions for Review will not be published (App. G at 90a; App. H at 91a). The two opinions of the Arizona Tax Court (App. C at 28a; App. D at 67a) are reported at *Bohn v. Waddell,* 164 Ariz. 74, 790 P.2d 772 (Tax 1990) and *Bohn v. Waddell,* 167 Ariz. 344, 807 P.2d 1 (Tax 1991), respectively. The Judgment of the Arizona Tax Court is in App. F at 84a.

JURISDICTION

The Arizona Court of Appeals issued its decision in *Estate of Bohn* on September 29, 1992, affirming in part and vacating in part the judgment of the Arizona Tax Court. (App. A at 2a). On October 2, 1992, the Court of Appeals dismissed the *Abbott* appeal as moot due to the decision in *Estate of Bohn.* (App. B at 26a).

On October 28, 1992, the petitioners filed timely Petitions for Review with the Arizona Supreme Court, seeking to secure the reversal of the Court of Appeals decision. The Arizona Supreme Court denied the Petitions for Review on April 14, 1993. (App. G at 90a; App. H at 91a). Petitioners thereupon filed this Petition within the time allowed by law. Jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

4 U.S.C. § 111 provides in pertinent part:

> The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States . . . by a duly con-

> stituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

28 U.S.C. § 1341 provides:

> The district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State.

42 U.S.C. § 1983 provides in pertinent part:

> Any person who, under color of any statute . . . of any State . . ., subjects or causes to be subjected, any citizen of the United States . . . to the deprivation of any rights, privileges or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, suit in equity or other proceeding for redress.

The Supremacy Clause of the United States Constitution, Article VI, Cl. 2, provides in pertinent part:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; . . . shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any thing in the Constitution or Laws of any State to the Contrary notwithstanding.

The Due Process Clause of the United States Constitution, Amendment XIV, § 1, provides in pertinent part:

> No state shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty or property without due process of law . . . .

Pertinent provisions of Arizona's Constitution, statutes and regulations are set forth in App. J at 155a and App. O at 176a.

STATEMENT OF THE CASE

This case arises in the wake of this Court's decision in *Davis v. Michigan Dep't of Treasury*, 489 U.S. 803 (1989). In *Davis*, this Court held that the tax system of Michigan, which discriminated in favor of retired state and local government employees and against retired federal employees, was invalid under 4 U.S.C. § 111. Arizona, like Michigan, measures state taxable income by starting with federal adjusted gross income. Thus federal and state pensions are both in the tax base. Like Michigan, Arizona exempted the entirety of retired local government employees' retirement compensation while at the same time taxing virtually all of federal employees' retirement compensation. Ariz. Rev. Stat. Ann. § 43-1001 and § 43-1022(3) and (4) (1980) (amended 1989). (App. J at 161-62a; App. C at 29a).[1]

Shortly after the announcement of the *Davis* decision, the Arizona Department of Revenue ("Department") announced that it would continue to collect the Arizona income tax imposed on federal pensions and impose penalties on those who did not timely pay (R. 273) and that it would await a judicial decision before recognizing any refund claims based on *Davis*. (App. C at 46a).

After the Department's announcement that refund claims would be denied and no relief provided until ordered by a court, this action was commenced in the Arizona Tax Court on May 1, 1989 by John L. Bohn (now deceased), his wife Shirley, Donald Rutan and his wife Mary, and Carl Linton, a single man. During the course of the proceedings below, the other 4,823 petitioners moved to intervene to ensure the protection of their legal rights, the tolling of the statute of limitations and the right to appear in the proceedings. The Tax

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[1] A $2,500 exemption was provided for federal civil service pensions paid under the federal civil service system. Military pensions and non-civil service pensions were fully taxed. *Id.*

Court denied the motion to intervene, invoking the doctrine of virtual representation advanced by the respondents. (App. E at 83a). The intervenors timely appealed the denial to the Arizona Court of Appeals in the *Abbott* proceeding.

The *Estate of Bohn* case proceeded with extended discovery, briefing and several hearings. During the course of the proceedings, the Department advised Arizona's retired federal employees that these proceedings would determine their right to a refund. (App. K at 166a). On April 6, 1990 the Arizona Tax Court declared, under Arizona's declaratory judgments act (rejecting any right to an injunction or declaration of illegality under 42 U.S.C. § 1983), that Arizona's tax on federal pensions violated 4 U.S.C. § 111. (App. C at 30a). The Tax Court held that petitioners were not entitled to an injunction to prevent the continued collection of the Arizona income tax because they had a refund right under Arizona law. (App. C at 46-47a). However, the Tax Court announced that the refund to which federal retirees were entitled was not the amount of the tax exacted on federal pensions, but only the amount by which federal retirees were "damaged" by the illegal taxation, the "damages" being calculated by the Court's assuming the imposition of a hypothetical tax on retired Arizona employees and estimating the tax reduction which all Arizona taxpayers (including petitioners) would have enjoyed had the hypothetical tax been imposed on and collected from state retirees. (App. C at 54-60a). The Tax Court found that Arizona had no administrative process in place which could provide an adequate remedy and that no Arizona administrative body had the power to determine that an Arizona tax statute was unconstitutional. (App. C at 45-46a).

After a series of motions following the Tax Court's first Opinion,[2] the Tax Court entered its judgment on

[2] This Court's decision in *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco, etc.*, 496 U.S. 18 (1990), was announced after

March 7, 1991. (App. F at 89a). Petitioners filed a timely appeal to the Arizona Court of Appeals on March 11, 1991. Petitioners sought, *inter alia*, a reversal of the Tax Court's hypothetical refund remedy and its refusal to certify the petitioner class. On March 18, 1991, the respondents timely cross-appealed asserting, *inter alia*, that *Davis* was not retroactive, that the state's discrimination against retired military personnel was not precluded by 4 U.S.C. § 111, that no refunds should be paid even if *Davis* were retroactive and, alternatively, asserted that this case should be dismissed on jurisdictional grounds. The Court of Appeals consolidated the *Abbott* and *Estate of Bohn* proceedings for oral argument and consideration. (App. A at 7a).

On September 29, 1992 (App. A at 2a), the Arizona Court of Appeals vacated the Tax Court's opinions in *Estate of Bohn* because the Tax Court was without jurisdiction to entertain the action until after the petitioners had exhausted the administrative process created by its decision. (App. A at 24-25a).[3] On October 2, 1992, the Court of Appeals declared that the *Abbott* proceeding was mooted by its *Estate of Bohn* ruling.[3] (App. B at 27a).

Petitioners timely filed Petitions for Review with the Arizona Supreme Court on October 28, 1992, asserting, *inter alia*, that the Court of Appeals' newly-created ad-

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the first opinion of the Tax Court. After a motion for reconsideration by petitioners, on March 7, 1991 the Tax Court held in its Supplemental Opinion that *McKesson* was either inapplicable (App. D at 70a and 81a) or supported refunding less than all of the taxes illegally exacted (App. D at 82a).

[3] The decision of the Court of Appeals also purported to affirm some unidentified portion of the Tax Court's decision, a ruling at odds with the vacation on jurisdictional grounds. This combined vacation and affirmance renders the scope of the court's ruling doubtful and subjects petitioners to further uncertainty because of the potential for a state court to hold that some as yet unidentifiable portion of the decision is *res judicata*.

ministrative process was futile, useless, inadequate and constitutionally-deficient under the Fourteenth Amendment. The Supreme Court denied review on April 14, 1993.

REASONS FOR GRANTING THE WRIT

This case raises questions of substantial public importance concerning the propriety of states retaining taxes collected in violation of the Constitution and statutes of the United States. This case represents a variation of the recurring theme of the states denying federal rights by denying citizens a remedy for the states' violation of federal rights. Specifically, this case presents the interrelated questions of whether a state may change its remedial rules after the tax has been collected by imposing a remedial scheme that is wholly illusory—one that results in the unlawful exaction remaining in the state treasury, while denying citizens a real opportunity to protect the federal right. Review by this Court is necessary to resolve finally the issue of whether this Court's decisions in *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18 (1990) and *James B. Beam Distilling Co. v. Georgia*, —— U.S. ——, 111 S.Ct. 2439 (1991), may be subverted through the charade of state remedies which do not satisfy constitutional standards.

1. This petition is the eleventh to be filed within the last two terms challenging a state's refusal to refund taxes collected in violation of the intergovernmental tax immunity doctrine.[4] Several of these petitions involve the

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[4] *See Pledger v. Bosnick*, No. 91-375 (Arkansas); *Barker v. Kansas*, No. 91-611, *rev'd*, —— U.S. ——, 112 S. Ct. 1619 (1992); *Harper v. Virginia Dep't of Taxation*, No. 91-794, *cert. granted*, 112 S. Ct. 1934 (1992); *Colorado v. Kuhn*, No. 91-980, *cert. dismissed*, 112 S. Ct. 1925 (1992); *Swanson v. North Carolina*, No. 91-1436; *Sheehy v. Montana Dep't of Revenue*, No. 91-1473; *Bass v. South Carolina*, No. 91-1697; *Norwest Bank Duluth, N.A. v.*

question of whether this Court's decision in *Davis v. Michigan Dep't of Treasury*, 489 U.S. 803 (1989), may be applied nonretroactively so as to defeat federal retirees' entitlement to refunds of unconstitutional state taxes imposed upon their federal annuities. At least four of these petitions, including the petition in this case, pose the directly related question of whether states may achieve the same result—a denial of relief—under the guise of a constitutionally deficient state remedy.[5] In addition, this issue is currently being raised by the states upon remand in both *Beam*[6] and *Barker*.[7] Moreover, similar or identical issues are also currently pending before state courts in two other intergovernmental tax immunity cases. *See Comerica Bank-Detroit v. Michigan Dep't of Treasury*, 194 Mich. App. 77, 486 N.W.2d 338 (Ct. App.), *application for leave to appeal held in abeyance*, 495 N.W.2d 382 (Mich. 1992);[8] *Kerr v.*

Minnesota Comm'r of Revenue, No. 91-2047; *Duffy v. Wetzler*, No. 92-521 (New York); and *Reich v. Collins*, No. 92-1276 (Georgia).

[5] *See, e.g., Bass v. South Carolina, supra*; *Norwest Bank Duluth, N.A. v. Minnesota Comm'r of Revenue, supra*; *Reich v. Collins, supra.*

[6] *See, e.g., Reich v. Collins*, No. 92-1276, pet. at 13.

[7] In *Barker*, the State asserted during oral argument that a decision in favor of military retirees would obligate it to refund 91 million dollars to the members of the certified class. (Official Transcript, March 3, 1992, p. 38-39). The State also acknowledged that there was no protest requirement conditioning the right to refunds in Kansas and that this Court's decision in *Barker* would govern all members of the class. *Id.* at 39-40. Yet, on remand, the state of Kansas is now attempting to play the same game that Arizona has played here. *See Barker v. Kansas*, District Court of Shawnee County, Kansas Division Four, Nos.: 89-CV-666 and 1100 (consolidated), Defendants' Motion to Dismiss Plaintiffs' Claims for Income Tax Refunds, dated Dec. 1, 1992.

[8] The *Comerica Bank-Detroit* case, like the *Norwest Bank* case, also involves 31 U.S.C. § 742 as construed by this Court in *Memphis Bank & Trust Co. v. Garner*, 459 U.S. 392 (1983). In *Comerica Bank-Detroit*, the Michigan Court of Appeals, followed *Beam*,

Waddell, No. 1 CA-TX 92-0010, *appeal pending* (Az. Ct. App.).[9]

Accordingly, while analytically different from the retroactivity issue *sub judice* in *Harper*, this petition presents the same ultimate question of whether states may render the enforcement of federal rights inutile by denying citizens a remedy for the states' violations of federal rights. Until definitive guidance is provided by this Court, state courts will continue to struggle with this issue under its new guise of constitutionally deficient state remedies.[10] Review by this Court is thus necessary to

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applied *Memphis Bank* retroactively, but remanded to the trial court for reconsideration of remedy. *Comerica Bank-Detroit*, 486 N.W.2d at 343.

[9] In its recently filed appellate brief in *Kerr*, Arizona is now asserting that the rights of the certified class of 42,500 current federal employees in *Kerr* are barred under the *Bohn* decision. *See* Defendants-Appellees' Combined Response and Opening Brief on Cross-Appeal, dated January 19, 1993. The Arizona Tax Court held in *Kerr* that Arizona law violates 4 U.S.C. § 111 because it discriminates in favor of *current* state employees and against *current* federal employees. However, the Tax Court refused to give its decision retroactive effect, reasoning that *Davis*, although decided in 1989, was irrelevant to the question of retroactivity because the discrimination in *Kerr* was on current compensation, not on pension income. In the Tax Court's view, this was a "new rule of law," which the Tax Court concluded permitted it to set an effective date for its decision, even though Arizona continued the discrimination against federal employees for over two years after *Davis*. After declaring that the Arizona tax discriminated against federal employees in December of 1990, the Arizona Tax Court held that Arizona law was only "illegal" after April, 1991, thereby allowing the state to collect an additional year of illegal taxes--1990--from federal employees.

[10] In the wake of *Beam*, the states quickly realized that they could no longer rely on the prospectivity defense to defeat the enforcement of federal rights. *See, e.g., Robinson v. City of Seattle*, 119 Wash. 2d 34, 830 P.2d 318, 339-43, *cert. denied*, 113 S. Ct. 676 (1992) (following *Beam* and abolishing the rule of selective prospectivity originally announced in *National Can Corp. v. Washington Dep't of Revenue*, 109 Wash. 2d 878, 749 P.2d 1286, *cert. denied*,

resolve this question of demonstrated difficulty and importance.

2. In *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18 (1990), this Court reaffirmed the principle " 'that a man who denies the legality of a tax should have a clear and certain remedy.' " *Id.* at 32, quoting *Atchison, T. & S.F.R. Co. v. O'Connor*, 223 U.S. 280 (1912).[11] Here, the petitioners invoked the clear and certain remedy available to them under settled Arizona law and tried the case to final judgment before the Arizona Tax Court.[12] During the pendency of

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486 U.S. 1040 (1988)). Indeed, upon the completion of briefing and oral argument before this Court in *Harper*, state taxing authorities conceded that it was unlikely that a prospectivity analysis of *Davis* was warranted. They also acknowledged that it was doubtful that *Davis* satisfied the threshold test for prospectivity. *See* HARPER ORAL ARGUMENT ADDRESSES TAXPAYER REMEDY, Tax Administrators News, December, 1992 at 137. However, these state authorities were also quick to point out that hope was not lost because there was now a new game: "procedural bars" to remedies. *Id.* at 144.

[11] Arizona imposes civil and criminal penalties to insure taxpayer compliance with its income tax laws. Among other sanctions, Arizona imposes penalties and interest for the failure to pay taxes on their due date, Ariz. Rev. Stat. Ann. §§ 42-134 and 42-136. App. J at 159-61a. It also purports to prohibit injunctions to prevent the collection of taxes. Ariz. Rev. Stat. Ann. § 42-124(B)(1). App. J at 159a. Criminal sanctions are also imposed. Ariz. Rev. Stat. Ann. § 42-137. App. J at 161a. Whatever remedies the respondents may claim exist, Arizona's personal income tax law places taxpayers at a " 'serious disadvantage' ". *McKesson*, 496 U.S. at 38 n.21 (citation omitted). Indeed, as a matter of state law, tax schemes imposing comparable penalties are "coercive". *Duhame v. State Tax Comm'n*, 65 Ariz. 268, 179 P.2d 252 (1947).

[12] Under the Arizona Constitution, the Tax Court was vested with original jurisdiction of this case. Ariz. Const. Art. IV, § 14 is explicit: "The Superior Court shall have original jurisdiction of . . .: (2) cases of equity and at law which involve . . . the legality of any tax." App. J at 155a. *See also* A.R.S. §§ 12-123(A); 12-161(A). App. J at 155-56a. *See also Tafflin v. Levitt*, 493 U.S. 455, 458 (1990) ("[S]tate courts have inherent authority, and are

the proceedings before the trial court, the State informed all 70,000 members of the virtually represented federal retiree class that "[t]his lawsuit will determine whether or not the state must refund any taxes paid on these benefits in past years." App. K at 166a. However, on appeal, the Arizona Court of Appeals held, in an unprecedented decision, that the Arizona Tax Court could not entertain the petitioners' claims for relief.

The members of the petitioner class have been deprived of their property without ever having been afforded " 'a clear and certain remedy.' " *McKesson*, 496 U.S. at 32 (citation omitted). The arbitrary result reached by the Court of Appeals here is analogous to the result rejected by this Court in *Brinkerhoff-Faris Trust & Sav. Co. v. Hill*, 281 U.S. 673, 682 (1930) ("[A] State may not deprive a person of all existing remedies for the enforcement of a right . . . ."). Here, however, the result is even more egregious because the new state remedy not only forecloses the rights of the petitioner class, but also, if permitted to stand, will foreclose all opportunity to defend against any form of unconstitutional exaction by the State of Arizona.[13] Moreover, if this decision is permitted to stand, it will only be a matter of time before other states replicate Arizona's ruse of the illusory remedy —a remedy which insures that all unlawful exactions

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thus presumptively competent, to adjudicate claims arising under the laws of the United States").

[13] As discussed below, as the result of the Court of Appeals decision in this case, there is no clear and certain remedy available in Arizona to enforce the Constitution, enactments of Congress or decisions of this Court limiting the state's power to tax. For example, this Court's pronouncements in *McKesson, supra*; *Davis v. Michigan Dep't of Treasury*, 489 U.S. 803 (1989); *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984); and *Aloha Airlines, Inc. v. Director of Taxation of Hawaii*, 464 U.S. 7 (1983), cannot be enforced under Arizona's illusory scheme and are meaningless in Arizona because there is no remedy to prevent a violation of the rights secured under these decisions.

remain in the state treasury. Indeed, the Arkansas General Assembly recently considered such a remedial scheme. H.B. 1827 (Ark. 79th Gen. A/Reg. Sess. 1993), if it had been enacted, would have eviscerated a state remedy for unconstitutional taxes.[14] Review by this Court is essential to prevent the states from transforming the Supremacy Clause into a meaningless promise.

The practical effect of the Court of Appeals decision is to deprive the 70,000 members of the petitioner class of all remedies for the enforcement of their rights without ever having afforded the members of the class the opportunity to be heard. Upon the announcement of Arizona's new remedial scheme, the petitioners sought timely and immediate review by the Arizona Supreme Court of the deprivation created by the Court of Appeals' decision. Such review was denied. App. G at 90a; App. H at 91a. The remedy created by the Court of Appeals has been cut from whole cloth and even if it were now available to some members of the petitioner class, this remedy is constitutionally deficient.

In relegating the petitioners to an implied exhaustion requirement, the Court of Appeals, *inter alia,* ignored the Tax Court's determination that there was "no administrative process in place that would provide an adequate remedy . . . [and that] an administrative body has no power to determine [that] a taxing statute is uncon-

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[14] The bill passed the House but was defeated by the state Senate. It is anticipated that this Bill will be reintroduced when the Arkansas General Assembly reconvenes in late May. Section 2 of H.B. 1827 provides:

> (k) Upon the entry of a final order by a court of competent jurisdiction that a tax statute or regulation, in whole or in part, is invalid or unconstitutional as applied, under the United States Constitution or the Arkansas Constitution, an amended return or verified claim for refund of an overpayment of state tax under such invalid or unconstitutional statute or regulation may only be made for a tax which becomes due and payable following the entry of such order.

stitutional." App. A at 11a.[15] Instead, the Court of Appeals held that an administrative body has the power to consider and decide the constitutionality of legislative enactments. This holding cannot withstand scrutiny.

It is a familiar tenet of administrative law that "[o]nly the courts have authority to take action which runs counter to the expressed will of the legislature," K. Davis, *Administrative Law Text,* § 20.04 at 388-89 (3d ed. 1972). Arizona is no exception. Under Arizona law, "the constitutionality of [a statute] is strictly a judicial question." *State ex rel. Davis v. Osborne,* 14 Ariz. 185, 188, 125 P. 884 (1912). This purely judicial power may not be conferred on an administrative body. *Batty v. Arizona State Dental Bd.,* 57 Ariz. 239, 112 P.2d 870, 873 (1941) ("[T]he term 'judicial' powers as used in constitutional provisions like sec. 1, art. 6 of our Constitution, on both reason and authority, includes only those powers which as a matter of law can be conferred only on courts as such . . . .").

Under the Arizona Constitution and settled state law, the petitioners properly invoked the only state remedy available to them. The Tax Court had jurisdiction under Ariz. Const. Art. IV, § 14(2). It also had jurisdiction under A.R.S. § 12-1831, *et seq.* (App. O at 176a), to

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[15] The record establishes that the defendants refused to stop the enforcement of the tax in issue. R. 126. In addition, at the time this case was commenced, the Arizona Board of Tax Appeals ("BOTA") was without jurisdiction to entertain the petitioners' claims. *See Chase Dist. v. Arizona Dep't of Revenue,* [1956-1989 Transfer Binder—New Matters] Ariz. Tax Rep. ¶ 200-824 (CCH) (Ariz. Bd. of Tax App., June 7, 1988); *Dar-Mel, Inc. v. Arizona Dep't of Revenue,* [1956-1989 Transfer Binder—New Matters] Ariz. Tax Rep. ¶ 200-854 (CCH) (Ariz. Bd. of Tax. App., February 7, 1989); *Ryan v. Arizona Dep't of Revenue,* 2 Ariz. Tax Rep. ¶ 200-897 (CCH) (Ariz. Bd. of Tax. App., November 11, 1989); and *Lloyd Constr. Co. v. Arizona Dep't of Revenue,* 2 Ariz. Tax Rep. ¶ 200-895 (CCH) (Ariz. Bd. of Tax. App., November 28, 1989).

determine the invalidity of the tax in issue. *See State Tax Comm'n v. Wallapai Brick & Clay Prod., Inc.*, 85 Ariz. 23, 330 P.2d 988 (1958); *Kelly v. Bastedo*, 70 Ariz. 371, 220 P.2d 1069 (1950); *Peterson v. Central Ariz. Light & Power Co.*, 56 Ariz. 231, 107 P.2d 205 (1940). *Cf. State Compensation Fund v. Symington*, 113 Ariz. Adv. Rep. 29, 1993 WL 54250 (1993) (special action invalidating an Arizona tax scheme under the Arizona Constitution and enjoining its enforcement). It is also clear under A.R.S. § 12-1838 (App. O at 176a) that the Tax Court properly exercised its jurisdiction to determine all issues in the case. *Cf. Mosher v. Lount*, 33 Ariz. 272, 278, 264 P. 68 (1928) ("Our courts, having taken jurisdiction of a matter, will render whatever judgment may be necessary to settle the issues and rights of the parties, whether they be equitable or legal."); *Vargas v. Superior Court*, 60 Ariz. 395, 138 P.2d 287 (1943).

As the result of the Court of Appeals decision in this case, the petitioners have been denied "the only remedy ever available for the enforcement of [their] right," *Brinkerhoff-Faris Co.*, 281 U.S. at 679, to recover the taxes unlawfully exacted. This deprivation was not cured by Arizona's new illusory remedy.

Because of the Eleventh Amendment and the Tax Injunction Act, 28 U.S.C. § 1341, *Davis*-related claimants as the petitioners are relegated exclusively to state courts to press their claims for refunds. But it is these courts that have demonstrated the greatest difficulty in applying the Fourteenth Amendment. This Court is the only federal court that can hear the retirees' claims. Review by this Court is thus necessary to assure a correct and evenhanded application of this Court's decisions to all federal retirees. Absent review by this Court, "[t]he State too easily avoids its responsibilities, and . . . go[es] its way unimpeded and unburdened with any remedy for those who have been wronged during the period of

[Arizona's] noncompliance with federal law." *Green v. Mansour*, 474 U.S. 64, 81 (1985) (Blackmun, J., dissenting).

3. Arizona's newly announced remedial scheme fails to satisfy the requirements of due process. Review by this Court is necessary to provide guidance to the states that uncertain and illusory remedies do not satisfy "minimum federal requirements." *McKesson*, 496 U.S. at 51-52. In addition, review is necessary to reverse the decision of the Arizona Court of Appeals, which, in fact, has permitted the State of Arizona in this case to appropriate the property of the petitioners "arbitrarily and without due process of law." *McKesson*, 496 U.S. at 33, quoting *Ward v. Love County Bd. of Comm'rs*, 253 U.S. 17, 24 (1920).

Arizona's new remedy is no remedy at all. Under the Court of Appeals' decision, the petitioners are required to seek relief from the Arizona Department of Revenue ("Department"). However, there are no time limits within which the Department must act and the Department has no rules governing the prosecution and resolution of claims such as those in issue in this case. App. J at 163a.[16] It is only if and when the claim is in fact ultimately denied by the Department and its Director that the taxpayer is permitted to proceed to BOTA.[17] A.R.S.

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[16] A.R.S. § 42-130(B) (App. J at 159a) provides that if the Department does not take action within six months after the taxpayer submits his refund claim, the taxpayer may treat the claim as disallowed, *but* must then appeal, *within the Department* for an internal hearing. A.R.S. § 42-122. App. J at 157-58a. No time limit whatsoever is prescribed by which the Department must hold such a hearing or take action, or after which the Department is deemed to have rejected the taxpayer's claim.

[17] BOTA's jurisdiction is limited to appeals from final decisions of the Department. *Keystone Graphics, Inc. v. Arizona Dep't of Revenue*, [1956-1989 Transfer Binder—New Matters] Ariz. Tax Rep. ¶ 200-817 (CCH) (Ariz. Bd. of Tax App., April 20, 1988).

§ 42-124 (A). App. J at 158a. There is no time limit within which BOTA must act.

In addition, BOTA is an administrative body staffed by part time hearing examiners. Historically, it has processed on average less than a hundred cases per year [18] and its backlog of pending appeals has increased each year. App. M at 170a. If BOTA were to process the cases of the 70,000 members of the class at its historic rate, it would take over 700 years to exhaust the new remedial process.[19]

In *Coit Indep. Joint Venture v. FSLIC*, 489 U.S. 561, 586 (1989), the Court held that an administrative process, which does not establish time limits for the consideration of claims, fails to comport with due process. In *Coit*, the statutory scheme at issue required a claimant to first submit its claim to FSLIC for determination before seeking judicial relief. Although FSLIC was required to either allow, disallow or retain a claim "for further review" within six months, there was no time limit established for claims retained for "further review." The Court held: "These procedures give FSLIC virtually unlimited discretion to bury large claims like [claimants'] in the administrative process, and to stay judicial proceedings for an unconscionably long period of time . . ." *Id.* at 586. Observing that claimant's claim had "essentially been relegated to a 'black hole' from which it may not emerge . . .", *id.*, the Court held that the administrative process was inadequate and exhaustion was ex-

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[18] The respondents assert that there is no class action remedy before the Department of Revenue or BOTA. BOTA has never adopted rules of procedure governing class actions.

[19] Moreover, if the Court of Appeals subjects the 42,500 member class in *Kerr v. Waddell* to the same remedy, the process would take over 1,200 years to exhaust. This, of course, assumes that BOTA does nothing on the cases properly within its limited jurisdiction. *See* note 9, *supra*.

cused, citing *Greene v. United States*, 376 U.S. 149, 163 (1964). *Id.* at 587.[20]

The Due Process Clause of the Fourteenth Amendment also requires that a tribunal be impartial. In *Withrow v. Larkin*, 421 U.S. 35 (1975), the Court stated that "a biased decisionmaker [is] constitutionally unacceptable." *Withrow*, 421 U.S. at 47. "This applies to administrative agencies which adjudicate as well as to courts." *Id.* at 46, citing *Gibson v. Berryhill*, 411 U.S. 564, 579 (1973). The Court stated further that "various situations have been identified in which experience teaches that the probability of actual bias on the part of the . . . decisionmaker is too high to be constitutionally tolerable." *Withrow*, 421 U.S. at 47. The Court noted that among these cases are those in which the "adjudicator has . . . been the target of personal . . . criticism from the party before him." *Id.*

In the instant action, injunctive relief was sought against the respondents. Moreover, this litigation has been aggressively pursued by the petitioners and vigorously defended by the respondents. The Court of Appeals' new remedy requires the petitioners to go before the very decisionmakers who have been the target of personal criticism, who have already adversely decided the matter, and who can delay resolution of petitioners' claims indefinitely before petitioners are entitled to seek judicial relief. Requiring exhaustion under Arizona's new remedy here would violate the Due Process Clause of the Fourteenth Amendment.

Moreover, even if it were assumed that BOTA now has the power to adjudicate the issue of the constitu-

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[20] *See also Gibson v. Berryhill*, 411 U.S. 564, 575 n.14 (1973) (administrative remedy deemed inadequate "[m]ost often . . . because of delay by the agency:); *Smith v. Illinois Bell Tel. Co.*, 270 U.S. 587, 591-92 (1926) (claimant "is not required indefinitely to await a decision of the rate-making tribunal before applying to a federal court . . .").

tionality of Arizona's discriminatory scheme, the administrative process is nevertheless inadequate and exhaustion is excused as a matter of law because the administrative agency lacks the "authority to grant the type of relief requested." *McCarthy v. Madigan,* 112 S. Ct. 1081, 1088 (1992). *See also McNeese v. Board of Educ.,* 373 U.S. 668, 675 (1963) (students seeking to integrate public school need not file complaint with school superintendent because the "Superintendent himself apparently has no power to order corrective action" except to request the Attorney General to bring suit); *Montana Nat'l Bank of Billings v. Yellowstone County,* 276 U.S. 499, 505 (1928) (taxpayer seeking refund not required to exhaust where "any such application [would have been] utterly futile since the county board of equalization was powerless to grant any appropriate relief.").[21]

If the Court of Appeals' new remedial scheme were to be applied to the petitioners' claims, the claims would now be subject to A.R.S. § 35-196.03, which was enacted after the commencement of this case. App. J at 157a. Under A.R.S. § 35-196.03, BOTA has no power to authorize a refund remedy for "invalid" or unconstitutional taxes. By purporting to condition the refund right for "invalid" taxes upon a legislative appropriation, the remedial scheme, which the Court of Appeals announced must be exhausted, is inadequate as a matter of law. *Standard Oil Co. of New Jersey v. Fox,* 6 F. Supp. 494, 498 (S.D. W. Va. 1934), *rev'd on other grounds,* 294 U.S. 87 (1935) ("How this right is to be exercised is not made definite; nor is it made clear how the taxpayer,

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[21] Of course, in the instant case, the illusory remedy is also futile. The respondents have steadfastly maintained that they will grant no relief. R. 126. *See City Bank Farmers' Trust Co. v. Schnader,* 291 U.S. 24, 27 (1934) (exhaustion unnecessary where Secretary of Revenue advised taxpayer that his claim would be denied).

if successful in a suit brought for the purpose, may recover back his money.")[22]

In addition, under the Court of Appeals' new remedial scheme it is uncertain whether the petitioners ever can obtain the requisite judicial declaration of invalidity which is a condition of obtaining a legislative appropriation under A.R.S. § 35-196.03. If petitioners were to successfully pursue their refund claims before BOTA under its newly created jurisdiction, the only relief available would be a determination that petitioners were entitled to relief. However, under the decision below, in order to obtain a judicial declaration of invalidity, it would be necessary to obtain judicial review of BOTA's favorable determination. This would require that the petitioners invoke the appellate jurisdiction of the Tax Court under A.R.S. § 42-124 (B) in order to obtain judicial review. App. J at 158-59a. However, under the decisional law it is unclear whether a prevailing party before an administrative body can satisfy the appellate jurisdictional requisite of an "aggrieved party." *See Burmister v. City of Prescott*, 38 Ariz. 66, 69, 297 P. 443 (1931). Thus, the Court of Appeals' new remedy is, at best, uncertain. Indeed, it is the very Catch-22 it was intended to be in order to defeat the enforcement of these federal rights.[23]

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[22] A.R.S. § 35-196.03, *inter alia*, does not specify a procedure for a taxpayer to obtain such an appropriation, provides no right to compel an appropriation, does not specify a time limit for payment, makes no provision for the payment of interest, and presumably is subject to legislative contest and gubernatorial veto. In addition, it is uncertain whether, after judicial relief is obtained, one appropriation may be obtained for the entire class or whether each member of the class would be required to seek the enactment of 70,000 individual appropriations.

[23] Assuming that the numerous constitutional infirmities in the new scheme could be overcome, it is still inadequate. A.R.S. § 35-196.03 purports to require the petitioners, even if successful, to submit to the expense, burden and delay of four *de novo* proceedings—one before the Department, one before its Director, one before BOTA and a fourth—a trial—before the Tax Court in order

In addition to the numerous flaws in the administrative process legislated by the decision below, there is yet another compelling reason why review must be granted here to reverse the decision below. Applying the requisite level of scrutiny—" 'intensely practical' ", *McCarthy*, 112 S. Ct. at 1087, to the analysis of the Court of Appeals, it is clear that the end sought by the decision is not a legitimate one. The imposition of the illusory new remedy seeks only to find "an easy way . . . to prevent the enforcement of . . . the Fourteenth Amendment . . . ." *General Oil Co. v. Crain*, 209 U.S. 211, 226 (1908).

However, as observed by this Court in *McCarthy*, "administrative procedures *must 'not* be used to harass or otherwise discourage those with legitimate claims.' " *McCarthy*, 112 S. Ct. at 1088 (emphasis added) (quoting *Patsy v. Florida Int'l Univ.*, 634 F.2d 900, 912-13 (Former 5th Cir. 1981), *rev'd on other grounds, sub nom., Patsy v. Board of Regents of Florida*, 457 U.S. 496 (1982)).

4. Review by this Court is also necessary to resolve the conflict among the state courts of last resort in *Davis*-related cases. In contrast to the decision in the instant case, the Supreme Court of Colorado, consistent with well-settled principles, held that the enforcement of a federal right in state court cannot be foreclosed by the imposition of a futile and/or inadequate remedy. *See Kuhn v. State, Dep't of Revenue*, 817 P.2d 101, 104 (Colo. 1991), *cert. dismissed*, 112 S. Ct. 1925 (1992)

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to satisfy the statute's requirement of a court's final judgment. Even after this process, relief is uncertain because of the separate appropriation requirement. However, "[a] remedy at law cannot be considered adequate . . . unless it covers the entire case . . . ." *Township of Hillsborough v. Cromwell*, 326 U.S. 620, 629 (1946). *Cf. Garrett v. Bamford*, 538 F.2d 63, 71 (3d Cir.), *cert. denied*, 429 U.S. 977 (1976) ("Where legal remedies require multiple suits involving identical issues against the same defendant, federal equity practice has recognized the inadequacy of the legal remedy and has provided a forum.").

("A party challenging the constitutionality of a statute need not first exhaust the administrative remedies provided in the statute."). *Cf. Pledger v. Bosnick*, 811 S.W.2d 286, 293 (Ark. 1991), *pet. for cert. filed*, 60 U.S.L.W. 3173 (U.S. Sep. 3, 1991) (No. 91-375); *Sizemore v. Rinehart*, 611 So. 2d 1064, 1068 (Ala. Civ. App. 1992), *writ quashed as improvidently granted, sub nom., Ex Parte Sizemore*, 611 So. 2d 1069 (Ala. 1993).

5. The result reached by the Arizona Court of Appeals also discriminates based on the origin of the petitioners' claims. In Arizona, taxpayers seeking to enforce rights secured under the Arizona constitution are assured a clear and certain judicial remedy. *State Compensation Fund v. Symington*, 133 Ariz. Adv. Rep. 29, 1993 WL 54250 (1993). A state remedial scheme that provides a clear and certain remedy for claims based on state law but denies that right to taxpayers seeking to enforce constitutional rights is unconstitutional. *See McKnett v. St. Louis & S.F.R. Co.*, 292 U.S. 230, 234 (1934) ("A state may not discriminate against rights arising under federal laws."). *Cf. Hathorn v. Lovorn*, 457 U.S. 255, 263 (1982); *NAACP v. Alabama*, 357 U.S. 449, 457 (1958).

As the result of the decision below, petitioners had no "clear and certain" remedy for the unconstitutional taxes they were compelled to pay. Thus, even if the court below were correct in legislating its new remedy, petitioners nonetheless would be entitled to relief directly under the Fourteenth Amendment.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari to the Court of Appeals of the State of Arizona, Division One, should be granted.

Dated: April 30, 1993

Respectfully submitted,

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APPENDICES

APPENDICES

APPENDIX A

IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

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1 CA-TX 91-008

DEPARTMENT T

ESTATE OF JOHN L. BOHN, SHIRLEY BOHN, DONALD and MARY RUTAN, husband and wife, and CARL LINTON, a single man,
Plaintiffs-Appellants,
Cross Appellees,

v.

PAUL WADDELL, individually and as Director of the Department of Revenue of the State of Arizona; DEPARTMENT OF REVENUE OF THE STATE OF ARIZONA, and CRAIG CORMIER, individually and as the Assistant Director of the Arizona Department of Revenue, *et al.*,
Defendants-Appellees,
Cross Appellants.

Appeal from the Arizona Tax Court

Cause No. TX 89-00050

The Honorable William T. Moroney, Judge

AFFIRMED IN PART;
REVERSED IN PART; REMANDED

Opinions of the Arizona Tax Court
164 Ariz. 74, 790 P.2d 772 (Tax Ct. 1990) and
167 Ariz. 344, 807 P.2d 1 (Tax Ct. 1991)

VACATED

OPINION

[Filed Sep. 29, 1992]

TOCI, Judge

During the tax years 1984 through 1988, Arizona's income tax laws exempted from income taxation 100% of state, county, and municipal retirement benefits paid to retired employees of those political entities, while exempting only the first $2,500 of federal retirement benefits paid to retired federal employees.

On March 28, 1989, the United States Supreme Court, in *Davis v. Michigan Dep't of Treasury*, 489 U.S. 803 (1989), invalidated a similar Michigan income tax scheme on the ground it violated the principles of intergovernmental tax immunity.

One month later several retired federal employees sued the Arizona Department of Revenue, claiming that the Arizona exemption statutes violated federal law. Although it declined to issue injunctive relief to the taxpayers, the tax court agreed. It concluded that the statutory scheme taxing federal pensions violated federal law because it did not tax state pensions in the same way. The tax court adopted a refund formula that refunded to federal retirees a small percentage of the taxes they paid on federal retirement benefits.

We hold that the tax court did not abuse its discretion in declining to issue injunctive relief to the taxpayers under 42 U.S.C. section 1983. We also hold, however,

that the plaintiff-taxpayers' failure to exhaust their Arizona administrative remedies either in their individual or representative capacities prevented the tax court from ruling on their claims for Arizona income tax refunds. Accordingly, we vacate the tax court's opinions. In so doing, we do not reach the question of the propriety of the tax court's refund formula.

Because of our holding, we also need not determine the remaining issues concerning the scope and retroactivity of the United States Supreme Court's decision in *Davis*. Similarly, we do not reach the question whether the taxpayers' attorneys are entitled to an award of attorney's fees under the "common fund" theory.

ISSUES

(1) Were the taxpayers subjected to irreparable injury by the tax court's refusal to grant injunctive relief when the Department of Revenue announced that, despite the March 28, 1989 holding in *Davis*, it would penalize any federal employee who did not pay the Arizona income tax on federal pensions paid in 1988?

(2) Were the taxpayers required to exhaust their administrative remedies? To determine this issue, we must decide the following subordinate issues:

(a) Is the statutory refund scheme mandatory, or does the tax court have original jurisdiction of tax refund claims?

(b) Is it proper for an administrative agency to apply a constitutional doctrine to a state of facts before it?

(c) Was administrative review futile, thereby excusing the taxpayers from exhausting their administrative remedies?

FACTS AND PROCEDURAL HISTORY

A. The Tax Court's Ruling Below

After the *Davis* decision, Arizona taxpayers Jack and Shirley Bohn, Donald and Mary Rutan, and Carl Linton filed a complaint in the Maricopa County Superior Court. They filed for themselves and all other residents of Arizona who received United States government retirement benefits during the period in question. The suit claimed that Ariz. Rev. Stat. Ann ("A.R.S.") section 43-1022(4)[1] violated federal law.

The complaint named the director and former directors of the Arizona Department of Revenue and their spouses as defendants. Invoking 42 U.S.C. section 1983 as authority for the action, it sought declaratory and injunctive relief, damages of "all monies unlawfully paid to or collected by the defendants under the authority of A.R.S. § 43-1022 . . .," and attorney's fees and costs.

The defendants moved to dismiss the complaint or alternatively for summary judgment. The taxpayers filed a cross-motion for summary judgment, for declaratory and

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[1] A.R.S. § 43-1022 provided in part:

In computing Arizona adjusted gross income, the following amounts shall be subtracted from Arizona gross income:

. . . .

2. Contributions made to the state retirement system, the corrections officer retirement plan, the public safety personnel retirement system, the elected officials' retirement plan or a county or city retirement plan.

3. Benefits, annuities and pensions received from the state retirement system, state retirement plan, the corrections officer retirement plan, the public safety personnel retirement system, the elected officials' retirement plan or a county or city retirement plan.

4. Income received as annuities under the United States civil service retirement system from the United States government service retirement and disability fund, in an amount of not to exceed two thousand five hundred dollars.

injunctive relief, and for class certification. *See* Ariz. R. Civ. P. 23(b)(2). The tax court granted the taxpayers' motion to amend their complaint to add the Department as a defendant and to state a separate claim for refund of Arizona income taxes paid on federal retirement benefits for the tax years in question.

After hearing argument on the cross-motions for summary judgment and the taxpayers' motions for class certification and declaratory and injunctive relief, the tax court: (1) granted appellees' motion to dismiss the taxpayers' damages claim under 42 U.S.C. section 1983; (2) denied the taxpayers' motion for injunctive relief; (3) treated military retirement pay the same as federal civil service retirement benefits; (4) held that the statutory scheme taxing federal pensions violated federal law because it did not tax state pensions in the same way; (5) granted plaintiffs refunds measured by "the difference between the tax federal pensioners paid on their pensions and what they would have paid had state taxpayers been similarly taxed"; (6) directed the Department to propose a refund plan consistent with that principle; and (7) announced it would not certify a class, provided the Department could devise an administrative plan to effectively administer the refund process under the doctrine of virtual representation.

Following these rulings, appellees moved to dismiss the taxpayers' second amended complaint. Their motion cited numerous grounds, including the theory that the tax court lacked jurisdiction of the refund claims because the taxpayers did not follow statutory administrative procedures. After briefing, the tax court denied the motion.

As directed, the Department submitted a proposed refund plan to the tax court. It designed the plan to operate with the named plaintiffs as "virtual representatives" of all nonparty taxpayers rather than as representatives of the putative class. After the parties had briefed the refund

issue, the taxpayers' counsel filed a series of motions to join successively increasing numbers of named individuals as parties plaintiff. Each motion stated that it would be withdrawn if the court ultimately granted the taxpayers' pending motion for class certification. The tax court denied the motions.

B. The First Opinion

On April 6, 1990, the tax court published its formal opinion pursuant to A.R.S. section 12-171. *See Bohn v. Waddell*, 164 Ariz. 74, 790 P.2d 772 (Tax 1990). Instead of permitting the case to proceed as a class action, the court adopted the "virtual representation" approach the Department proposed. Nevertheless, it rejected appellees' contention that the taxpayers' claim for refunds should be dismissed for failure to exhaust administrative remedies. Finally, the tax court explained in detail the legal theory supporting its decision to award an economic remedy, and the method of calculating each taxpayer's refund.

C. Events After the First Opinion

After the tax court filed its opinion, some 4,500 individual Arizona taxpayers, represented by the taxpayers' counsel, filed a motion to intervene as parties plaintiff. Characterizing the motion as having been filed "at this late date," the tax court denied it. The intervenors timely appealed from the tax court's formal order denying intervention. This court docketed their appeal as case No. 1 CA-TX 90-029.

The taxpayers moved for reconsideration, for a new trial, or alternatively to alter or amend the judgment. They also moved for an award of attorney's fees and expert witness fees. The taxpayers later requested clarification of the tax court's opinion, moved for an order withdrawing the tax court's opinion from publication, and moved for relief from the judgment.

The tax court denied the taxpayers' motions. It also declined to award attorney's fees to the taxpayers' counsel under the private attorney general doctrine or the "common fund" doctrine. Instead, it awarded the taxpayers attorney's fees limited to $105,000, plus costs, under A.R.S. section 12-348.

D. The Supplemental Opinion

On March 7, 1991, the tax court issued a supplemental opinion that reaffirmed its original opinion of April 6, 1990. *See Bohn v. Waddell*, 167 Ariz. 344, 807 P.2d 1 (Tax 1991).[2] When the tax court issued its supplemental opinion, it simultaneously entered a final judgment approved by both sides as to form.

The taxpayers filed a timely notice of appeal. Appellees filed a timely notice of cross-appeal. We have jurisdiction pursuant to A.R.S. section 12-2101(B).[3]

DISCUSSION

I. The Law of Intergovernmental Tax Immunity

A long-standing principle once prohibited states from taxing federal instrumentalities. *See McCulloch v. Maryland*, 17 U.S. 316 (1819) (discriminatory tax on United

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[2] The supplemental opinion primarily concerned the taxpayers' attack on the tax court's decision to grant them less than a full refund of taxes paid on federal pensions. The taxpayers relied on *McKesson Corp. v. Florida Div. of Alcohol & Tobacco*, 496 U.S. 18, (1990), *American Trucking Ass'n., Inc. v. Smith*, 496 U.S. 167 (1990) (plurality opinion), *Ashland Oil, Inc. v. Caryl*, 497 U.S. 916 (1990), and *National Mines Corp. v. Caryl*, 497 U.S. 922 (1990). The tax court determined that none of these decisions supported the taxpayers' renewed bid for a full refund.

[3] By order of July 31, 1991, this court consolidated the oral arguments in 1 CA-TX 90-029 and 1 CA-TX 91-008. Both appeals were assigned to Department T of this court pursuant to A.R.S. §§ 12-120.04 and 12-170(C).

States bank unconstitutionally interfered with federal powers). This principle became known as the doctrine of intergovernmental tax immunity. At one point, the doctrine expanded to the point that neither federal or state governmental entities could tax the employees of the other. *See Collector v. Day*, 78 U.S. 113, 124-28 (1870) (invalidated federal income tax on state judge); *Dobbins v. Commissioners of Erie County*, 41 U.S. 435 (1842) (invalidated state tax on federal officer).

Later, courts began to limit the doctrine of intergovernmental tax immunity. *See Helvering v. Gerhardt*, 304 U.S. 405 (1938) (permitted nondiscriminatory federal tax on state pensions); *Graves v. New York ex rel. O'Keefe*, 306 U.S. 466, 486-87 (1939) (permitted nondiscriminatory state tax on federal employees). Furthermore, when Congress passed the Public Salary Tax Act of 1939, it specifically codified the requisite nondiscriminatory treatment for intergovernmental taxation. *See* 4 U.S.C. § 111.[4]

The United States Supreme Court invalidated Michigan's income tax scheme under these principles. *See Davis*, 489 U.S. 803. It held that Michigan's tax laws unconstitutionally discriminated against individuals receiving federal retirement benefits. Michigan did not tax state and local retirement benefits, but it did tax federal civil service retirement benefits to the extent they exceeded $8,000 annually. The Supreme Court held this violated 4 U.S.C. section 111 and the principles of intergovernmental tax immunity. *See id.*, 489 U.S. at 817. When the plaintiff-taxpayers challenged the similar Arizona tax scheme, they relied on the holding in *Davis*.

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[4] 4 U.S.C. § 111 provides in pertinent part:

The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States . . . by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

II. Tax Court's Refusal To Issue Injunctive Relief

The taxpayers contend that the tax court abused its discretion when it refused to enjoin the individual appellees from enforcing the former Arizona statutory scheme that taxed federal retirement benefits differently from state retirement benefits. We do not agree. The tax court correctly found that the taxpayers had failed to demonstrate they would suffer irreparable harm unless injunctive relief was granted.

As the tax court noted, the Arizona legislature amended the statute shortly after the *Davis* decision to bring it into compliance with that decision.[5] *See* 1989 Ariz. Sess. Laws ch. 312, § 12. The state now taxes individuals receiving government pensions similarly, regardless of the pensions' origin. Abandonment of a challenged practice is an important factor in determining whether the tax court should have issued an injunction. *See City of Mesquite v. Aladdin's Castle, Inc.*, 455 U.S. 283, 289 (1982) (though defendant's voluntary cessation of challenged practice does not deprive court of power to determine its legality, cessation is important factor bearing on whether court should exercise discretion to enjoin defendant from renewing practice). Under the statutory scheme as it now applies to tax years after 1988, no discriminatory taxation of the type condemned in *Davis* can occur under color of Arizona law.

Also, the tax court declined to enjoin further efforts by the individual appellees to collect income taxes on federal and military retirement benefits for tax years 1984 through 1988. The tax court based this ruling on these grounds:

> This Court has determined as excessive only a small portion of the income tax assessed an individual

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[5] A.R.S. section 43-1022(2) now subtracts the first $2,500 of federal, military, state, and local retirement benefits from Arizona adjusted gross income. This results in nondiscriminatory taxation of federal and military retirement benefits.

> federal retiree in recent years. A taxpayer who, as a result of the Department's continuing collection effort, pays a tax that is later determined to be illegal as a result of the decision in *Davis* may have it refunded with interest. Suspending, or otherwise inhibiting, the Department's tax collection effort against all federal retirees would result in little ultimate benefit to the federal retiree taxpayer, even if preventing some illegal tax collection was the result. On the other hand, a serious disruption in the conduct of the Department's business could occur. This would be to the detriment of, not only the Department, but all non-federal retiree taxpayers in the state.

Bohn, 164 Ariz. at 88, 790, P.2d at 786.

Even if we assume that the taxpayers are entitled to refunds, we do not reach that issue here, they did not show a need for injunctive relief. For the period 1984 through 1988, any affected taxpayers could have filed administrative refund claims with the Department of Revenue or protested assessments of unpaid taxes on federal or military retirement income. In fact, as of May 23, 1989, the taxpayers filed between 20,000 and 25,000 "protective" claims for refund. They could have pursued all properly filed claims or protests through the administrative process and into the superior court. *Cf. Weinberger v. Romero-Barcelo,* 456 U.S. 305, 312-13 (1982) (injunction denied where other means available to ensure compliance with federal water pollution laws obviated necessity for injunction).

III. Taxpayers' Failure To Exhaust State Administrative Remedies

The Department argued that the tax court should have dismissed the taxpayers' claim for state income tax refunds for failure to exhaust administrative remedies. The tax court rejected that argument on two grounds. First, it concluded that because no administrative process was in place that would provide an adequate remedy, exhaustion of administrative remedies was not required. Second, the tax court held that an administrative body has no power to determine whether a taxing statute is unconstitutional.

We disagree with the tax court. We hold that the tax court lacks jurisdiction over any claim for refund of taxes that has not been first properly presented to the Department of Revenue and the Board of Tax Appeals. We reach this conclusion because a statutory income tax administrative refund claim and appeal process was available, as a prerequisite to judicial relief, to process the federal taxpayers' claims. We also hold that a taxpayer may present a constitutional challenge in the administrative proceeding for the purpose of reducing or correcting his or her assessment.

A. Exhaustion of Administrative Remedies

Our supreme court has recognized a public policy that discourages suits for the refund of taxes even when illegally collected. *Univar Corp. v. City of Phoenix*, 122 Ariz. 220, 223, 594 P.2d 86, 89 (1979); *Southern Pac. Co. v. Cochise County*, 92 Ariz. 395, 406, 377 P.2d 770, 778 (1963). At common law, taxes voluntarily paid could not be recovered. *Southern Pac. Co.*, 92 Ariz. at 406, 377 P.2d at 778. Accordingly, if parties have statutory recourse to an administrative agency that has authority to grant appropriate remedies, they must scrupulously follow the statutory procedures. If they fail to fully utilize all their administrative remedies, the superior

court lacks jurisdiction to consider their claim. *See Univar Corp.*, 122 Ariz. at 223, 594 P.2d at 89; *Mountain View Pioneer Hosp. v. Employment Sec. Comm'n*, 107 Ariz. 81, 85, 482 P.2d 448, 452 (1971) ("When a party fails to exhaust all his administrative remedies . . . the trial court is without jurisdiction . . . ."); *Williams v. Bankers Nat. Ins. Co.*, 80 Ariz. 294, 297 P.2d 344 (1956); *Oliver v. Arizona Dep't of Racing*, 147 Ariz. 83, 708 P.2d 764 (App. 1985).

Under the exhaustion doctrine, litigants may not seek "judicial relief for a supposed or threatened injury until the prescribed administrative remedy has been exhausted." *Myers v. Bethlehem Shipbuilding Co.*, 303 U.S. 41, 50-51 (1938). The rationale behind this doctrine permits "an administrative agency to perform functions within its special competence—to make a factual record, to apply its expertise, and to correct its own errors so as to moot judicial controversies." *Parisi v. Davidson*, 405 U.S. 34, 37 (1972). This doctrine promotes judicial and administrative efficiency.

Courts have characterized the exhaustion rule as a rule of judicial administration that is usually applied by virtue of express statutory mandate. *Campbell v. Mountain States Tel. & Tel. Co.*, 120 Ariz. 426, 429, 586 P.2d 987, 990 (App. 1978). However, our supreme court has held that the rule is not merely discretionary, but rather jurisdictional. *Mountain View Pioneer Hosp.*, 107 Ariz. at 85, 482 P.2d at 452. It also stated:

> [I]f the taxpayer desires to raise a question as to his taxes he is compelled to scrupulously follow the statutory procedures, *Smotkin v. Peterson*, 73 Ariz. 1, 236 P.2d 743 [1951], for the refund of taxes paid is by virtue of governmental grace rather than by reason of any legal right which the taxpayer has to such a refund. *State v. Airesearch Mfg. Co.*, 68 Ariz. 342, 206 P.2d 562 [1949].

Southern Pac. Co., 92 Ariz. at 406, 377 P.2d at 778. More recently, the Arizona Supreme Court has acknowledged statutory prerequisites taxpayers must exercise before judicial review of challenged taxation and refund claims. *See Pittsburgh & Midway Coal v. Department of Rev.*, 161 Ariz. 135, 136, 776 P.2d 1061, 1062 (1989) (all taxpayers contesting various taxes in consolidated appeals exhausted administrative remedies before judicial review).

Here, both parties agree that none of the named plaintiffs or members of the putative class exhausted their state administrative remedies before filing this action for a refund. The taxpayers argue that they did not need to exhaust administrative remedies. Relying on the state constitution, the taxpayers contend that the superior court had original jurisdiction to hear their claims. This contention is misplaced. The constitutional provision on which they rely provides in part:

> The superior court shall have original jurisdiction of:
> . . . .
> 2. Cases of equity and at law which involve the title to or possession of real property, or the legality of any tax, impost, assesment, toll or municipal ordinance.

Ariz. Const. Art. 6, § 14(2); *see also* A.R.S. § 12-161.[6] Contrary to the taxpayers' position, this provision neither expressly nor impliedly prevents the legislature from conditioning the exercise of the superior court's jurisdiction on the taxpayers' exhausting available administrative reme-

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[6] A.R.S. § 12-161. Definition of tax court

A. In this chapter, unless the context otherwise requires, "tax court" means the tax department of the superior court in Maricopa county when exercising the original jurisdiction of the superior court over cases of equity and at law which involve the legality of any tax, impost or assessment.

B. This court shall be known as the Arizona tax court.

dies. *See Univar Corp.*, 122 Ariz. at 223, 594 P.2d at 89. *Cf. Pritchard v. State*, 163 Ariz. 427, 430, 788 P.2d 1178, 1181 (1990) (legislative divestiture of superior court jurisdiction must be clear and unimbiguous); *Daou v. Harris*, 139 Ariz. 353, 356, 678 P.2d 934, 937 (1984).

Furthermore, in *State Tax Comm'n v. Superior Court*, 104 Ariz. 166, 450 P.2d 103 (1969), our supreme court stated:

> We further hold that where taxes appear to have been imposed under semblance of authority and adequate remedies have been delineated in the taxing Statutes, the taxpayer must pursue such remedies to secure relief.

Id., 104 Ariz. at 169, 450 P.2d 106.

The legislature chose to create a statutory scheme that required the taxpayers to seek refunds of income taxes paid on federal retirement benefits. The rationale supporting the exhaustion doctrine is a practical one:

> The main purpose in requiring an administrative hearing is to remove the onus of a great volume of complicated tax cases from unnecessary judicial review and to initially place them before a specialized tribunal trained to handle such matters.

Mountain View Pioneer Hosp., 107 Ariz. at 85, 482 P.2d at 452.

B. The Administrative Remedy

The applicable statute provides in part:

> Within the time limits in § 42-115 [four years from date of return], a taxpayer who fails to protest the payment of any tax illegally or erroneously collected may file a claim for refund of the taxes paid. Such refund claim shall then be governed by § 42-130 and this section.

A.R.S. § 42-124(B)(2). The refund claim statute provides the administrative notice and procedural requirements.[7]

An individual taxpayer must petition for a hearing on the denial of a refund claim within ninety days from the date the Department mailed its notice of action. A.R.S. § 42-122(A). The Department must consider the petition and grant a hearing at the taxpayer's request. *Id.* The Department's order or decision on the petition becomes final thirty days after the taxpayer receives notice of the order or decision, "unless the petitioner appeals the order or decision to the state board [of tax appeals]." A.R.S. § 42-122(C); *see also* A.R.S. § 42-171.

The statutory scheme also sets out the procedure for tax appeals to the state board. The governing statute provides that an aggrieved taxpayer may appeal to the state board of tax appeals within thirty days after receiving the decision or order being appealed.[8] The unsuccessful

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[7] A.R.S. § 42-130 provides:

> A. If the department disallows any claim for refund, it shall notify the taxpayer accordingly. The department's action on the claim is final unless the taxpayer appeals to the department in writing within the time and in the manner prescribed by § 42-122. If the department disallows interest on any claims for refund, it shall notify the taxpayer accordingly and thereafter the claim shall be treated as a claim for refund.
>
> B. If the department fails to mail notice of action on any claim for refund of tax or interest within six months after the claim is filed, the taxpayer, prior to mailing of notice of action on the refund claim, may consider the claim disallowed. The taxpayer may appeal to the department for a hearing pursuant to § 42-122.

[8] A.R.S. § 42-124 provides, in part:

> A. A person aggrieved by a final decision or order of the department under this article may appeal to the state board by filing a notice of appeal in writing within thirty days after the receipt of the decision or order from which the appeal is taken. The board shall take testimony and examine documentary evidence as necessary to determine the appeal, all pursuant to administrative rules

party at the state tax board may then appeal to superior court. A.R.S. § 42-124(B)(2).

The statutory administrative refund claim and appeal process is not optional. Only one statute expressly authorizes a taxpayer to bring an action in the superior court to dispute Arizona income taxes. *See* A.R.S. § 42-124 (B). This section describes such actions exclusively as "appeals" to be heard and determined by the superior court as trials *de novo* from decisions of the Board of Tax Appeals. *See id.*

C. Exception to Exhaustion Rule

We now turn to the question whether one of the recognized exceptions to the doctrine of exhaustion of administrative remedies permits the taxpayers to file the refund claim directly in the superior court. For the reasons stated below, we find that none of the exceptions applies to excuse the taxpayers from exhausting their administrative remedies.

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to govern such appeals. On determining the appeal the board shall issue a decision consistent with its determination. The board's decision is final on the expiration of thirty days from the date when notice of its action is received by the taxpayer, unless either the department or the taxpayer brings an action in superior court as provided in subsection B.

B. The department or a taxpayer aggrieved by a decision of the board may bring an action in superior court subject to the following provisions:

. . . .

2. . . . In the case of income tax the taxpayer may bring an action against the department in superior court without paying the tax, penalty or interest under protest. The action shall not begin more than thirty days after the order or decision of the board becomes final. Failure to bring the action within thirty days constitutes a waiver of the protest and a waiver of all claims against this state arising from illegality in the tax, penalties and interest so paid. . . . The superior court shall hear and determine the appeal as a trial de novo. Either party to such action may appeal to the court of appeals or supreme court as provided by law.

We also observe that the supreme courts of Oregon and Wisconsin have both dismissed *Davis*-related refund class actions because the plaintiffs failed to exhaust applicable administrative remedies. *Nutbrown v. Munn*, 311 Or. 328, 811 P.2d 131 (1991), *cert. denied*, —— U.S. ——, 112 S. Ct. 867 (1992); *Hogan v. Musolf*, 163 Wis. 2d 1, 471 N.W.2d 216 (1991), *cert. denied*, —— U.S. ——, 112 S. Ct. 867 (1992).[9] The reasoning of those opinions is consistent with our rationale and holding in this case.

The doctrine of exhaustion of administrative remedies is subject to a limited number of recognized exceptions. When a statute expressly or impliedly authorizes a permissive administrative remedy, the exhaustion requirement does not apply. *Campbell v. Chatwin*, 102 Ariz. 251, 257, 428 P.2d 108, 114 (1967). Also, a court should not summarily apply the doctrine when a party challenges the agency's jurisdiction. *Id.* (citing K. Davis, *Administrative Law Treatise*, § 20.01 [1958]). In addition, a party need not exhaust administrative remedies when doing so would cause irreparable harm, or if the agency's expertise is unnecessary. *Univar Corp.*, 112 Ariz. at 224, 594 P.2d at 90. Finally, the exhaustion requirement is inapplicable when the administrative process would be useless or futile under the circumstances. *See Minor v. Cochise Cnty.*, 125 Ariz. 170, 172, 608 P.2d 309, 311 (1980); *Zeigler v. Kirschner*, 162 Ariz. 77, 86, 781 P.2d 54, 63 (App. 1989).

1. Mandatory Administrative Remedy Could Determine Refund Issue

We have already rejected the taxpayers' contention that the available administrative remedies were merely permissive. We also conclude that the Department of Revenue and the Board of Tax Appeals have authority to consider the constitutionality of a tax statute.

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[9] The plaintiff-taxpayers in both these cases were represented by lead counsel for the taxpayers in the instant case.

The taxpayers contend that the agencies in the Department of Revenue cannot consider constitutional questions even when they perform their statutory quasi-judicial function. We specifically rejected a similar argument in *Valley Vendors Corp. v. City of Phoenix*, 126 Ariz. 491, 616 P.2d 951 (App. 1980). In that case, the City of Phoenix assessed sales and use taxes against the taxpayer. Instead of challenging the assessment administratively, the taxpayer sued directly in the superior court. The complaint alleged a discriminatory assessment of sales and use taxes, as well as double taxation. The plaintiff sought to have the city's use tax declared "void, illegal and unconstitutional" and enjoined its assessment. 128 Ariz. at 492, 616 P.2d at 952. One of the grounds for dismissing the complaint was the taxpayers' failure to exhaust administrative remedies. *Id.*

This court held that the taxpayer could have indeed raised constitutional issues in the City's administrative process. We stated:

> The basic issue to be tried is whether the taxpayer has been illegally taxed. *See* Phoenix City Code section 14-29(g), (e). The questions included within this issue can be wide-ranging and could very well include constitutional challenges. . . . Under section 14-29, . . . there is no limitation upon the grounds that the taxpayer may present to reduce or correct his assessment. As long as he asserts these grounds in the petition, they are preserved for an action in superior court.

126 Ariz. at 494, 616 P.2d at 954 (citations omitted). *See also Moki Mac River Expeditions*, 160 Ariz. 366, 372, 773 P.2d 474, 477 (App. 1989) (Board of Tax Appeals erroneously concluded transaction privilege tax violated the Commerce Clause because the taxpayer did not have enough business contacts with Arizona). Furthermore, the procedure upheld in *Valley Vendors* con-

tains very similar language to the tax refund procedure challenged in this case. 126 Ariz. at 492, 616 P.2d at 952. Likewise, here the statute does not limit the grounds that the appellants may raise in the refund process. *See* A.R.S. §§ 42-124 and -130.

We also reject the taxpayer's argument that *Arizona Corp. Comm'n v. Tucson Gas, Elec. Light & Power Co.*, 67 Ariz. 12, 189 P.2d 907 (1948) and *Manning v. Reilly*, 2 Ariz. App. 310, 408 P.2d 414 (1965), stand for the proposition that exhaustion of administrative remedies is not required. In *Tucson Gas* the court stated: "The Corporation Commission apparently knew it had no right to construe the constitutionality of [the statute], it being its duty to assume the law was constitutional." 67 Ariz. at 14, 189 P.2d at 908. This statement is pure dictum, without any citation of supporting authority. We conclude it has little precedential value.

In addition, *Manning* is not on point. There, the issue was whether a zoning ordinance was properly enacted. Division Two observed that the zoning board of adjustment had the traditional limited power to issue variances of the zoning code, but no power to determine the constitutionality of the zoning ordinance. 2 Ariz. App. at 312, 408 P.2d at 416. The court concluded it would serve no purpose to require one to exhaust administrative remedies when the board of adjustment could not pass on the constitutionality of the enactment of the zoning ordinance. *Id. Manning* does not cast doubt on our more-recent decision in *Valley Vendors*.

The taxpayers also cite a Board of Tax Appeals' decision in support of their argument that the agency cannot decide their refund claims because resolution would involve constitutional claims. *See Chase Distrib. v. Arizona Dep't of Revenue*, No. 489-86-S, slip op. at 2 (Ariz. Bd. of Tax App., June 7, 1988). However, the taxpayers' argument fails to draw a critical distinction.

Professor Davis' *Administrative Law Treatise* recognizes the distinction we draw here:

> *A fundamental distinction must be recognized between constitutional applicability of legislation to particular facts and constitutionality of the legislation.* When a tribunal passes upon constitutional applicability, it is carrying out the legislative intent, either express or implied or presumed. When a tribunal passes upon constitutionality of the legislation, the question is whether it shall take action which runs counter to the legislative intent. We commit to administrative agencies the power to determine constitutional applicability, but we do not commit to administrative agencies the power to determine constitutionality of legislation. Only the courts have authority to take action which runs counter to the expressed will of the legislative body.

Id., § 20.04, p. 74 (1958) (footnote omitted) (emphasis supplied). The Board of Tax Appeals' decisions impliedly acknowledge this distinction. While noting it does not have the power to declare statutes unconstitutional, the Board has nevertheless applied constitutional doctrines and federal law when resolving claims. *See, e.g., Tucson Mech. Contracting, Inc. v. Arizona Dep't of Revenue*, No. 607-88-S (Ariz. Bd. of Tax App., Nov. 28, 1989) (assessment against in-state contractors did not violate Equal Protection); *Lloyd Constr. Co. v. Arizona Dep't of Revenue*, No. 668-89-S (Ariz. Bd. of Tax App., Nov. 28, 1989) (alleged discriminatory enforcement of tax laws claimed to violate U.S. Constitution); *Ryan v. Arizona Dep't of Revenue*, No. 651-89-I (Ariz. Bd. of Tax App., Nov. 11, 1989) (adopting federal tax code definition did not violate U.S. Constitution). Contrary to the taxpayers' assertion, the board could have applied constitutional doctrines to their refund claims. *Valley Vendors*, 126 Ariz. at 494, 616 P.2d at 954.

Finally, we observe that even where "[an] agency has no particular expertise to decide on the constitutionaltiy of its own enabling act and will not ordinarily rule on the issue in any event," exhaustion of remedies has still been required. *Weyerhaeuser v. Marshall*, 592 F.2d 373, 376 (7th Cir. 1978). *See, e.g., W.E.B. DuBois Clubs of America v. Clark*, 389 U.S. 309 (1967). Exhaustion permits the agency to "develop the factual record so that the court will not have to decide 'important and difficult' questions of constitutional law" in the absence of a factual background. *Id.* at 312. Furthermore, during administrative review "the agency may decide favorably to the aggrieved party on other grounds, thus mooting the constitutional issue and relieving the courts of the need to decide it." *Id.* Thus, even if the taxpayers were correct in their argument that constitutional doctrines cannot be applied by the Department, exhaustion of remedies would be appropriate.

Here, the taxpayers' challenged discriminatory taxation of their pension income. However, they also sought a refund of taxes they paid under the former statutory scheme. The issue involved the application of the constitutional doctrines and federal law in the *Davis* holding to each taxpayer's right to a refund. It was a proper subject for the administrative process.

2. *Administrative Appeal Process Would Have Been Useful, Not Futile*

The tax court concluded that the statutory administrative process would not and could not have provided the refunds the taxpayers were seeking. The tax court stated:

> Indeed, the only evidence on the point, proffered by the Plaintiffs, reflects just the opposite. The public comment on the *Davis* decision by the Department was that the Department would await a judicial determination before it would recognize any claim based on *Davis*.

Bohn, 164 Ariz. at 87, 790 P.2d at 785. *Cf. White Mountain Apache Tribe v. Hodel*, 840 F.2d 675, 677-78 (9th Cir. 1988) (exhaustion may not be required when administrative review futile because of preannounced decision by final administrative decison maker or existence of objective and undisputed evidence of administrative bias). We disagree with the trial court.

We hold that the Department's announcement in the early stages of the case that it would deny *Davis*-related tax refunds did not render the statutory administrative process futile. The Board of Tax Appeals, an independent agency not under the control of the Department of Revenue, is the final decision maker in the administrative process. The taxpayers did not raise any issue of bias on the part of the Board of Tax Appeals. We also conclude that the knowledge and experience of the Department of Revenue and the Board of Tax Appeals were both necessary and significant in resolving the taxpayers' claims.

The tax court cites *Town of Paradise Valley v. Golf Leisure Corp.*, 27 Ariz. App. 600, 557 P.2d 532 (1976), in support of its position. This case is not on point. In *Paradise Valley*, the town council had not established an administrative review procedure for its final actions. The town unsuccessfully argued that the claimant should have reapplied to the same town council for a zoning variance. This court held that reapplication would have been futile because it was physically impossible to grant relief given the unavailability of additional acreage. 27 Ariz. App. at 610, 557 P.2d at 542.

The taxpayers argue that because the Department publicly announced that it would deny any refunds in absence of a court order, the administrative process was futile. They also contend that the current and former directors of the Department of Revenue, originally sued in their individual capacity, were biased against them. The taxpayers claim that applying the doctrine of exhaustion of

remedies would violate their right to due proces. We disagree with taxpayers.

The Department's administrative hearing division was never given the opportunity to consider the refund question. The Department's director never had the benefit of the evidence, legal arguments and findings the departmental hearing process would have generated. Furthermore, the Board of Tax Appeals issues the final decision in the administrative appeal process. The record contains no evidence that the Board of Tax Appeals had prejudged the issue. The Board is independent of the Department of Revenue and not subject to its control. *See* A.R.S. § 42-171(A) (It is "an independent agency which shall not in any way be subject to the supervision or control of the department of revenue.").

We further reject any implication that the exhaustion requirement should not apply here because the administrative agencies' expertise was unnecessary. We take judicial notice that persons hearing administrative appeals within the Department of Revenue and the Board of Tax Appeals have considerable legal and factual knowledge and experience with tax-related issues.

Additionally, the refund claims would raise issues that necessarily present practical questions about the calculation and mechanics of any refunds. In *Valley Vendors,* we said "[a]nalysis and determination of these issues would seem particularly suited to examination by administrative tax specialists." *Id.*, 126 Ariz. at 494, 616 P.2d 954. The same considerations exist here.

3. *Effect of Putative Class Status*

The taxpayers further contend that they were excused from having to exhaust their available administrative remedies. In support, they rely on the class action allegations in their claim for tax refunds. Their contention is without merit.

The taxpayers' unsuccessful effort to seek class certification does not excuse their failure to exhaust administrative remedies. The rule requiring parties to exhaust administrative remedies extends to actions brought on behalf of a class. The cases generally agree that a class action cannot be maintained unless at least one member of the putative class has exhausted appilcable administrative remedies. *Zeigler,* 162 Ariz. at 85, 781 P.2d at 62. The taxpayers cannot avoid this requirement simply because the tax court denied class certification. Even if the court had granted certification, at least one member would still be required to exhaust administrative remedies.

Here, a representative of the putative class could have exhausted appropriate remedies. *See Zeigler,* 162 Ariz. at 85, 781 P.2d at 62; *see also Lilian v. Commonwealth,* 467 Pa. 15, 354 A.2d 250 (1976) (class action for state tax refunds properly dismissed due to named plaintiffs' failure to follow statutorily prescribed administrative refund procedure); *Stenhouse v. Lynch,* 37 N.C. App. 280, 245 S.Ed.2d 830 (1978) (absent timely demand for refund, class action for refund of state income taxes properly dismissed). Alternatively, an administrative claim may be filed on behalf of a class under some circumstances. *See Andrew S. Arena, Inc. v. Superior Court,* 163 Ariz. 423, 788 P.2d 1174 (1990) (permitting a class claim against a public entity for building permit fees). None of the taxpayers exhausted the statutorily prescribed administrative refund procedure in this case.

CONCLUSION

We hold that the tax court erred when it did not dismiss the taxpayers' refund claim. Arizona law required the taxpayers to follow the administrative procedure to obtain a tax refund. None of the taxpayers exhausted available administrative remedies. No recognized exception to the exhaustion rule excused their failure to fol-

low the administrative refund procedure. Therefore, the tax court did not have subject matter jurisdiction.

Because of our holding, we do not decide the issue of whether the tax court erred when it refused to certify a plaintiff class, and instead relied on the doctrine of virtual representation for effecting refunds. Similarly, we do not approve of the tax court's refund formula.

We affirm the tax court's order denying injunctive relief. The tax court, however, should have dismissed the taxpayers' claims because they did not exhaust their administrative remedies. Because we reverse in part, we vacate the tax court's opinions below, and we remand for proceedings consistent with this opinion.

/s/ Philip E. Toci
PHILIP E. TOCI
Judge

CONCURRING:

/s/ Sarah D. Grant
SARAH D. GRANT
Presiding Judge

/s/ Jefferson L. Lankford
JEFFERSON L. LANKFORD
Judge

APPENDIX B

IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

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1 CA-TX 90-029

DEPARTMENT T

PAUL WADDELL, individually and as Director of the Department of Revenue of the State of Arizona; *et al.*,
Defendants-Appellees.

v.

ARTHUR J. ABBOTT, MARY L. ABBOTT, FRED ABENDSCHEIN, *et al.*,
Intervenors, Plaintiffs-Appellants.

Appeal from the Arizona Tax Court

Cause No. TX 89-00050

The Honorable William T. Moroney, Judge

DISMISSED

MEMORANDUM DECISION

[Filed Oct. 2, 1992]

The court, Presiding Judge Sarah D. Grant and Judges Jefferson L. Lankford and Philip E. Toci participating, has considered this appeal. For the reasons stated below, we dismiss the appeal as being moot.

Appellants, approximately 4,500 federal civil service retirees, sought to intervene in *Bohn v. Waddell,* Cause No. TX 89-0050. In *Bohn,* the plaintiff-taxpayers alleged that Arizona illegally taxed their federal retirement benefits from 1984 to 1988. Relying on *Davis v. Mich. Dep't of Treasury,* 489 U.S. 803 (1989) (state income tax scheme unconstitutionally taxed federal employees differently from state and local employees), the taxpayers sought refunds.

After the tax court denied the plaintiff-taxpayers' motion for class certification, the appellants moved to intervene in *Bohn.* Counsel for the named plaintiffs also represented the group seeking to intervene. The tax court denied their motions as untimely and ruled that the doctrine of virtual representation made class certification unnecessary. This appeal followed.

Ultimately, both parties appealed the tax court's decision in *Bohn. See Bohn v. Waddell,* 1 CA-TX 90-008 (filed September 29, 1992). In *Bohn,* we found that the plaintiffs failed to exhaust their administrative remedies. The tax court, therefore, lacked jurisdiction. Because of our holding in *Bohn,* appellants' claim that the tax court committed reversible error in denying their motions to intervene is rendered moot. Accordingly, we dismiss this appeal.

APPENDIX C

THE SUPERIOR COURT
OF THE STATE OF ARIZONA
IN THE ARIZONA TAX COURT

No. TX 89-00050

JOHN L. BOHN, *et al.*

v.

PAUL WADDELL, *et al.*

OPINION

On March 28, 1989, the United States Supreme Court rendered its decision in *Davis v. Michigan Department of Treasury*, ——– U.S. ——–, 109 S.Ct. 1500, 103 L.Ed.2d (1989). The *Davis* decision held, as contrary to federal law, certain provisions of Michigan law governing state taxation of income. Michigan imposed a tax on the pension benefits of federal retirees, while exempting from tax similar benefits enjoyed by State of Michigan pensioners.

There are five Plaintiffs herein. Two are retired United States military pensioners, one is a retired United States civil service pensioner, and two are spouses of the military retirees.

On May 1, 1989, Plaintiffs filed suit against the Director of the Department of Revenue, and all former Dierctors back through 1985. Plaintiffs alleged violations of 42 U.S.C. § 1983, and sought certification of a Plaintiff class of all federal pensioners who paid income tax to Arizona since 1985. The complaint sought a declaration

of unconstitutionality, injunctive relief, and damages measured by taxes paid to Arizona on federal pensions. The complaint, as first filed, did not name the State as a Defendant, nor did it make a claim for a tax refund.

Later, the complaint was amended to add a second count alleging as unconstitutional the statute by which Arizona taxed the Plaintiffs' federal pensions. The Department of Revenue was named as a Defendant. On the basis of this count, the Plaintiffs continue to press for a declaration of unconstitutionality, class certification, and injunctive relief. They also seek a refund of all taxes paid on federal pensions from 1984 on. In the amended complaint, the original complaint is repeated as Count 1. Both the original complaint, and the amended complaint are based on the *Davis* decision.

For all of the tax years material to the issues before the bench, Arizona gross income is equal to federal adjusted gross income. To determine Arizona adjusted gross income, subtractions authorized in A.R.S. § 43-1022 are made to Arizona gross income. Arizona adjusted gross income is further refined into Arizona taxable income, upon which Arizona income tax is assessed. As a result of the foregoing scheme, subtractions taken pursuant to A.R.S. § 43-1022 are exemptions from Arizona State income tax.

When the *Davis* decision was announced, A.R.S. § 43-1022(3) provided for a subtraction for all benefits from Arizona State retirement systems, and A.R.S. § 43-1022(4) provided for a subtraction for up to $2,500 of income from United States civil service retirement. There was no subtraction provided for pension benefits from any federal retirement program other than civil service. Military retirement income was not exempted from Arizona income tax, neither in whole nor in part.

Shortly after the *Davis* decision was announced, the Arizona legislature amended A.R.S. § 43-1022 to provide

a subtraction for up to $2,500 of income from all federal pensions and all state pensions. Laws, 1989, ch. 312 § 12, 1989 Ariz. Legis. Serv. 1604 (West). The subtraction previously allowed in A.R.S. § 43-1022(3) was repealed. This legislative change reduced the subtraction for state pensions and instituted a subtraction for non-civil service federal pensions so that all federal and state pensions are now treated the same. The amendment to A.R.S. § 43-1022 is effective for the tax year 1989 and subsequent years.

It is safe to say that the legislature was motivated by the *Davis* decision to make the change that it made to A.R.S. § 43-1022. It was the intent of the amendment to reform Arizona law so that it would comply with what was mandated by *Davis*: that is, that both federal and state pensions be treated the same.

The Court declares that the scheme for taxing federal and state pensions, as existed before the recent amendment to A.R.S. § 43-1022, was in violation of federal law, and further, was in violation of the federal constitutional doctrine of intergovernmental tax immunity.

The Court grants summary judgment to all Defendants on Count 1, holding such Defendants have an immunity from suit under 42 U.S.C. § 1983 because the acts complained of were all done in the performance of official duty, and the Plaintiffs' rights were not clearly established before the *Davis* decision.

The Court grants summary judgment to the Plaintiffs and against the Department of Revenue on Count 2 and makes such further orders in resolution of the Plaintiffs' suit as are reflected in this decision and in the Court's minute order of the same date.

The Court further holds that the Plaintiffs need not exhaust administrative remedies before bringing suit in this Court, and that Plaintiffs have failed to demonstrate the need for injunctive relief.

Pursuant to A.R.S. § 12-1841 and the doctrine of virtual representation, the Court directs the Department of Revenue to treat all persons who paid Arizona income tax on federal pensions for tax years 1984 through 1988 as though each such person were a Plaintiff herein. Because of the foregoing, the Court holds that certification of a Plaintiff class is neither necessary nor expedient.

The Department of Revenue is directed to refund a portion of Arizona income taxes paid by each Plaintiff, and all persons similarly situated, according to the following formula. In addition to the tax refund directed herein, the Department is to pay interest to each taxpayer at such rates as the Department pays when income tax overpayments are refunded.

To determine the amount of the refund due the taxpayer, two computations must be made. The first step is to multiply .0275 times the highest Arizona tax rate paid, times the taxpayer's federal pension income. If income has been subtracted pursuant to A.R.S. § 43-1022(4), the amount of such income multiplied by the taxpayer's highest Arizona rate must be subtracted from the amount determined in step one. No more tax can be refunded than was paid.

Refunds are to be made for tax years 1984 through 1988. Applications for such refunds may be made up until the first April 15th two years after this decision becomes final or until the expiration of the term provided in A.R.S. § 42-115, whichever is later.

In the balance of this opinion, the Court will discuss in detail the facts determined, and the law which applies.

Application of the Decision in *Davis* to the Arizona Scheme

Paul Davis, a resident of Michigan, received retirement benefits pursuant to the United States Civil Service Retirement Act. Michigan defined taxable income in a manner

that excluded all retirement benefits received from the state or its political subdivisions, but included federal retirement benefits. Davis sued the Michigan Department of the Treasury for "refunds of state taxes paid on his federal retirement benefits." *Davis*, 109 S.Ct. at 1503.

Davis claimed that the state's inconsistent treatment of state and federal retirement benefits discriminated against federal retirees in violation of 4 U.S.C. § 111. The United States Supreme Court, in an opinion written by Justice Kennedy, agreed with Davis.

4 U.S.C. § 111 was enacted as part of the Public Salary Tax Act of 1939. The purpose of the Public Salary Tax Act was to provide for federal income taxation of the salaries of state and local government employees. 4 U.S.C. § 111 states:

> The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States, a territory or possession or political subdivision thereof, the government of the District of Columbia, or an agency or instrumentality of one or more of the foregoing, by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

Justice Kennedy said the meaning of 4 U.S.C. § 111 is "unmistakable."

> It waives whatever immunity past and present federal employees would otherwise enjoy from state taxation of salaries, retirement benefits, and other forms of compensation paid on account of their employment with the Federal Government, except to the extent that such taxation discriminates on account of the source of the compensation.

Davis, 109 S.Ct. at 1505.

In analyzing the *Davis* opinion, one needs to consider that the typical American wage earner is subject to two governments, one the state, and one the United States. The immunity to which Justice Kennedy refers is an immunity from taxation by one government once enjoyed by the employees of the other government. This immunity was established as a corollary of the doctrine of intergovernmental tax immunity, a doctrine first advanced in *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819).

The tax immunity enjoyed by state and federal employees met its virtual demise in the late 1930's with decisions in *Helvering v. Gehrhardt*, 304 U.S. 405, 58 S.Ct. 969, 82 L.Ed. 1427 (1938), and *Graves v. New York ex rel. O'Keefe*, 306 U.S. 466, 59 S.Ct. 595, 83 L.Ed. 927 (1939). *Helvering* held that the United States could impose a tax on the salaries of state employees, and *Graves* held that states could impose a tax on the incomes of federal employees.

Most of the legislative process which resulted in the passage of the Public Salary Tax Act took place after *Helvering*, but before *Graves*. According to Justice Kennedy, Congress was uncertain just what immunity might still have been available to federal employees from state taxation of their income. 4 U.S.C. § 111 was enacted to expressly waive, on behalf of the United States, whatever immunity there was to non-discriminatory taxation.

4 U.S.C. § 111 did not, however, waive all immunity from state taxation of the income of federal employees. The final clause of the statute excepts from such waiver state income taxes which discriminate on the basis of the source of the federal employee's compensation.

In the *Davis* decision, the Supreme Court made three determinations that are important in applying the case to the Arizona income tax scheme. These determinations are:

> [One] The retention of immunity in § 111 is coextensive with the prohibition against discriminatory

> taxes embodied in the modern constitutional doctrine of intergovernmental tax immunity.
>
> *Davis*, 109 S. Ct. at 1506.
>
> [Two] Michigan's tax system discriminates in favor of retired state employees and against retired federal employees.
>
> *Id.* at 1507.
>
> [Three] The Michigan Income Tax Act violates principles of intergovernmental tax immunity by favoring retired state and local government employees over retired federal employees.
>
> *Id.* at 1508.

Davis suggests that the doctrine of intergovernmental tax immunity will not be violated if inconsistent tax treatment can be justified by "significant differences" between those favored and those not favored. *Id.* (citing *Phillips Chemical Co. v. Dumas Independent School Dist.*, 361 U.S. 376, 80 S.Ct. 474, 4 L.Ed.2d 384 (1960)). The opinion, however, does not identify any justifiable differences.

Michigan advanced as significant differences two circumstances. First, Michigan used the promise of income tax exemption of state pensions as an inducement to obtain and keep qualified civil servants. Second, federal pay and retirement benefits were substantially better than those of Michigan. The *Davis* Court rejected both of these arguments. Both of these arguments were made in the present case by the Department of Revenue.

The *Davis* opinion does not furnish a defined standard by which to determine what relationships need exist between classes of taxpayers in order for a state tax system to be discriminatory, and therefore violative of intergovernmental tax immunity. If the Michigan and Arizona schemes were the same, the similarity would be enough to declare the Arizona system flawed.

They are not the same, however. Michigan, as far as can be told from *Davis*, has only two classes of taxpayers whose benefits and liabilities have to be considered. Arizona has three.

"It is undisputed that Michigan's tax system discriminates in favor of retired state employees and against retired federal employees." *D*avis, 109 S.Ct. at 1507.

The foregoing statement contains all the rationale and all of the authority to be found in the *Davis* opinion for its affirmative holding that the Michigan system discriminates. Such an assertive pronouncement without further explanation shouts the obvious. Any difference in the tax treatment of government service retirees is a discrimination for purposes of 4 U.S.C. § 111.

The *Davis* opinion defines an appropriate remedy for Michigan to be "a mandate of equal treatment." *Id.* at 1509.

The income tax treatment of state and federal pensions cannot be equal if the treatment of all federal pensions is not the same. The Court finds that A.R.S. § 43-1022, subsections 3 and 4, discriminates in favor of Arizona State retirees, and against federal retirees. It also discriminates in favor of federal civil service retires, and against other federal retirees.

Pursuant to the Arizona Uniform Declaratory Judgment Act, A.R.S. § 12-1831 *et seq.*, the Court declares that so much of the Arizona State income tax system as was implemented by A.R.S. § 43-1022, subsections 3 and 4, as such statute existed prior to the tax year 1989, to have been in violation of 4 U.S.C. § 111, and in violation of the federal constitutional doctrine of intergovernmental tax immunity.

Motions for Summary Judgment

Count 1 of the amended complaint alleges claims against the individual Defendants based on a violation of 42 U.S.C. § 1983. According to the complaint, the individual Defendants, acting under color of state law and by dint of the enforcement power of the Arizona State income tax law, have imposed a tax on the Plaintiffs' federal pensions. Furthermore, say the Plaintiffs, these Defendants will continue to impose such a tax. The Plaintiffs claim such acts violate rights, privileges, and immunities guaranteed the Plaintiff's under the federal Constitution.

The Defendants filed a motion to dismiss the complaint, or in the alternative, for summary judgment. The motion was supported by affidavits. The motion was filed before the complaint was amended, when the only claim pressed by Plaintiffs was a § 1983 claim.

Plaintiffs responded to the Defendants' motion with a cross-motion for summary judgment. Plaintiffs also sought to amend the complaint, as indicated above. The motion to amend was granted. The Plainitffs' cross-motion for summary judgment was also supported by affidavits. Additional motions for summary relief were filed. In the course of further proceedings, much argument and authority on all issues were presented to the Court. Both parties had adequate opportunity to bring to the bench any matter they might have wished to present on the issues framed in the complaint. The Court considered the affidavits of the parties in deciding the motion and cross-motion. The Court therefore considers the motions to be cross-motions for summary judgment encompassing all claims set out in the amended complaint. Rule 12(b), A.R.C.P.; *Parks v. Macro-Dynamics, Inc.*, 121 Ariz. 517, 519-20, 591 P.2d 1005, 1007-08 (App. 1979).

The Plaintiffs' Section 1983 Claim

There are two considerations which bear upon an evaluation of the Plaintiffs' § 1983 claim. The legislative change in A.R.S. § 43-1022, which took place shortly after the Supreme Court opinion in *Davis* was published, removed as an issue in this litigation any purported civil rights violations for acts relative to tax years 1989 and after.

In addition, in all of their allegations claiming outrageous conduct by the Defendants, the Plaintiffs assume a right to total exemption from taxation of their pension income. The Court does not find that such a right exists.

In support of their motion, the Defendants argue the Court lacks jurisdiction because the Plaintiffs have failed to exhaust their administrative remedies. More will be said later about whether the Plaintiffs must exhaust administrative remedies as a pre-condition to their suit for a refund of an illegally collected tax. The Defendants' motion, however, was directed to Plaintiffs' § 1983 claim against the individual Defendants.

The recent decision of the Arizona Court of Appeals in *Zeigler v. Kirschner*, 162 Ariz. 77, ——, 781 P.2d 54, 55 (App. 1989) is dispositive of Defendants' argument. In *Zeigler*, the Court said, ". . . a state court may not condition a plaintiff's § 1983 rights upon the exhaustion of state administrative remedies."

In so ruling, the Court of Appeals relied on *Felder v. Casey*, 487 U.S. 131, 108 S.Ct. 2302, 101 L.Ed.2d 123 (1988); and *Patsy v. Board of Regents of Florida*, 457 U.S. 496, 102 S.Ct. 2557, 73 L.Ed.2d 172 (1982). Based on the foregoing authorities, this Court holds that the Plaintiffs need not exhaust administrative remedies before pursuing a claim against the individual Defendants premised on 42 U.S.C. § 1983.

In reviewing the original complaint, the one to which the Defendants' motion is addressed, this Court concludes

that it is directed at the individual Defendants in their individual capacities. The Department was not named as a Defendant, nor are allegations made which suggest that the thrust of Plaintiffs' claim for relief is directed at Defendants in their "official" capacity. Plaintiffs' memoranda in opposition to the Defendants' motion, and in support of their own motion for judgment is consistent with the Court's conclusion.

Nevertheless, certain allegations in the Plaintiffs' amended complaint might leave open the issue of whether the Plaintiffs make a claim against the state, or against the individual Defendants in their official capacity. Having thus waved at these issues in passing, the Court can now quickly put them to rest.

Throughout its long meandering course, federal civil rights law has struggled with whether a state is a person and thus subject to suit under § 1983. It has also wrestled with the dichotomy of official and individual capacities. *Monroe v. Pape*, 365 U.S. 167, 81 S.Ct. 473, 5 L.Ed.2d 492 (1961); *Fitzpatrick v. Bitzer*, 427 U.S. 445, 96 S.Ct. 2666, 49 L.Ed.2d 614 (1976); *Monell v. New York City Dep't of Social Servs.*, 436 U.S. 658, 98 S.Ct. 2018, 56 L.Ed.2d 611 (1978); *Kentucky v. Graham*, 473 U.S. 159, 105 S.Ct. 3099, 87 L.Ed.2d 114 (1985). *See also* the differing views of the justices in concurring and dissenting opinions in *Hutto v. Finney*, 437 U.S. 678, 98 S.Ct. 2565, 57 L.Ed.2d 522 (1978), and *Brandon v. Holt*, 469 U.S. 464, 105 S.Ct. 873, 83 L.Ed.2d 878 (1985).

A recent case from the United States Supreme Court, however, has settled both of these issues, at least for the time being. "Neither a state nor its officials acting in their official capacities are 'persons' under § 1983." *Will v. Michigan Dep't of State Police*, —— U.S. ——, 109 S.Ct. 2304, 105 L.Ed.2d 45 (1989). Based on *Will*, this Court holds that the Plaintiffs have no claim based on 42 US.C. § 1983 against the State or against the individual Defendants in their official capacities

The Court now considers the Plaintiffs' claim for money damages against the individual Defendants. These Defendants have raised the defense of a qualified immunity.

In *Scheur v. Rhodes,* 416 U.S. 232, 94 S.Ct. 1683, 40 L.Ed.2d 90 (1974), the United States Supreme Court was faced with the issue of whether state officials were immune as individuals from suits for damages pursuant to 42 U.S.C. § 1983. The officials in *Scheur* claimed immunity as to all acts performed within the scope of their official duties. The Supreme Court held that state officials in the executive branch of government did not have absolute immunity from suit in such a circumstance. The Court further held that such officials did have a qualified immunity from such suits, however.

The *Scheur* Court elected not to define "qualified immunity", but did suggest that it was based on a reasonable good faith belief that would justify the acts upon which the complaint was based. *Scheur,* 416 U.S. at 247-48.

42 U.S.C. § 1983 provides for a cause of action against officials of state government for alleged civil rights violations. In *Bivens v. Six Unknown Federal Narcotics Agents,* 403 U.S. 388, 91 S.Ct. 1999, 29 L.Ed.2d 619 (1971), the United States Supreme Court defined a cause of action against federal officials for the same conduct proscribed to state officials by § 1983.

In determining whether a qualified immunity exists, federal law does not distinguish between a § 1983 claim against state officials, or a *Bivens* type claim against federal officials. *Butz v. Economou,* 438 U.S. 478, 98 S.Ct. 2894, 57 L.Ed.2d 895 (1978); *Nixon v Fitzgerald,* 457 U.S. 731, 102 S.Ct. 2690, 73 L.Ed.2d 349 (1982).

Immunity defenses made in § 1983 claims are controlled by federal law. *Hampton v. City of Chicago,* 484 F.2d 602 (1973). The defense is an affirmative one that must be pleaded. *Gomez v. Toledo,* 446 U.S. 635, 100 S.Ct. 1920, 64 L.Ed.2d 572 (1980).

The standard for deciding whether a sued official is entitled to effectively assert a qualified immunity defense is an objective one. Government officials in the exercise of thier official duties are shielded from liability for civil damages if their conduct does not violate clearly established statutory or constitutional rights of which a reasonable person would have known. *Harlow v. Fitzgerald,* 457 U.S. 800, 815, 102 S.Ct. 2727, 73 L.Ed.2d 396 (1982). *See also Procunier v. Navarette,* 434 U.S. 555, 98 S.Ct. 855, 55 L.Ed.2d 24 (1978).

In *Davis v. Scherer,* 468 U.S. 183, 104 S.Ct. 3012, 82 L.Ed.2d 139 (1984), decided after *Harlow,* the United States Supreme Court stated: "A plaintiff who seeks damages for violation of constitutional and statutory rights may overcome the defendant official's qualified immunity only by showing that those rights were clearly established at the time of the conduct at issue." *Scherer,* 468 U.S. at 197.

The Court interprets this language to place the burden on the Plaintiff to establish that the rights which the Plaintiff claims were violated were rights that were clearly established at the time of the alleged violations.

In further defining qualified immunity, the Supreme Court said: "[t]he entitlement is an *immunity from suit* rather than a mere defense to liability; and like an absolute immunity, it is effectively lost if a case is permitted to go to trial." *Mitchell v. Forsyth,* 472 U.S. 511, 526, 105 S.Ct. 2806, 86 L.Ed.2d 411 (1985) (emphasis in original).

Defendants have pled the defense of a qualified immunity. All of the conduct of the Defendants of which the Plaintiffs complain was committed by the Defendants in the performance of their official duties as Directors of the State Department of Revenue. Indeed, all acts complained of were acts dictated by the then law of the State. Therefore, unless the allegedly violated rights of the Plaintiffs were clearly established at the time the alleged viola-

tions occurred, the Defendants are entitled to rely on their immunity defense.

Defendants are also entitled to an early resolution of the issue. *Mitchell,* supra. Plaintiffs have properly pled their § 1983 claim. *Gomez,* 446 U.S. at 640. Therefore whether Defendants' immunity defense is dispositive of Plaintiffs' § 1983 claim for damages cannot be resolved in a Motion to Dismiss. As previously indicated, however, the Court considers Defendants' motion as one for summary judgment.

The Plaintiffs bear the burden of demonstrating that the rights they claim were violated were rights clearly established at the time that the violations occurred. They have been given an adequate opportunity to advance whatever evidence on this point they deem to be appropriate.

Having properly raised a defense of qualified immunity, Defendants have a right to have the viability of the claimed defense determined at an early stage in the proceedings. Defendants have a right to have it determined before discovery on the merits. *Harlow,* 457 U.S. at 818.

Before a determination can be made whether rights were clearly established, the rights in issue must be identified. Actually, there is only one right involved here. Plaintiffs base thier § 1983 claim on *Davis v. Michigan.* The only right which the Plaintiffs could claim *Davis* defined for them was a right to have their federal pension benefits taxed the same as were state pension benefits.

Plaintiffs claim that Defendants knew, or should have known, that such a right was clearly established during the relevant tax years. In support of this position, Plaintiffs cite a report by a State Tax Commission accountant written in 1939, and a more recent expression of opinion by a State legislator. The report is too remote in time, and the legislator's opinion too removed from a Department director's employment universe, to be imputable to these Defendants. More importantly, such data is not relevant.

The determination of whether the right defined above was clearly established at the time the right was said to be violated is a matter of law to be determined by the Court. It is to be gauged on an objective standard. *Harlow*, 457 U.S. at 818.

The Arizona tax scheme, which the Court herein has declared to be in violation of federal law, was in place for a minimum of 25 years before *Davis*. There is no record that it ever was, before this lawsuit, attacked in any court. Justice Stevens, in his dissent in *Davis*, indicated that there were at least 14 states other than Michigan that granted tax benefits to state and local pensioners not granted to federal pensioners. *Davis*, 109 S.Ct. at 1511. Information supplied to the Supreme Court of Missouri indicates at least 21 states have similar provisions. *Hackman v. Director of Revenue*, 771 S.W.2d 77 (Mo. banc 1989) (Welliver, J., dissenting). The Plaintiffs provided an exhibit that suggests that as many as 23 states may be affected by the *Davis* decision.

The pervasiveness of the scheme, as well as its long life without challenge, are indications that the law which creates the right was not clearly established before *Davis*. These characteristics do not dispose of the issue, however.

If the language of the statute violated is unequivocal, considered in light of existent authority, and the impermissible act a plain violation, the prevalence of the wrong is not enough to overcome the certainty of the statutory language.

This Court must therefore consider, whether, as a matter of law, the plain language of 4 U.S.C. § 111 was such that a reasonable person would have known that the statute proscribed the disparate Arizona income tax treatment of state and federal pensions. The Court holds that it was not.

The statute reads, in relevant part:

> The United States consents to the taxation of pay or compensation for personal service as an officer or

> employee of the United States . . . if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

The statute does not address retirement income. It speaks of "pay" and "compensation for personal services" for "officers" and "employees," but does not specifically refer to income received by retired federal employees. The language of the non-discrimination clause is conditional, but it is not prohibitory. On its face, the statute does not conflict with pre-*Davis* A.R.S. § 42-1022.

Justice Kennedy, in writing for the Supreme Court in *Davis*, felt differently. He wrote, "the plain language of the statute dictates" that it applies to retired pay. *Davis*, 109 S.Ct. at 1504. Even so, this Court is of the view that, on this score, the statutory language leaves room for argument. Justice Kennedy acknowledged that Michigan's contention (that § 111 did not address retirement income), while hypertechnical, "was not inconsistent with the language" of the statute. *Id.*

Even if it were to have been clearly established before *Davis* that 4 U.S.C. § 111 included within its ambit retired pay, it was not clear that the Michigan scheme was an unconstitutional discrimination. The Supreme Court cites no precedent for its holding that virtually any difference is a discrimination under the statute. The Court further points out that discrimination under 4 U.S.C. § 111 is defined by a stricter standard than discrimination under the equal protection clause, from which most of the federal law interpreting discrimination has come. *Id.* at 1508. The justification for giving favorable tax treatment to state pensioners offered by Michigan in *Davis*, and the Department here (*see* page 8, *ante*), is sustainable under equal protection standards. *J.C. Penney Co. v. Arizona Dep't of Revenue*, 125 Ariz. 469, 610 P.2d 471 (App. 1980); *Flagstaff Vending Co. v. City of Flagstaff*, 118 Ariz. 556, 578 P.2d 985 (1978).

The *Davis* Court based its holding on "principles of intergovernmental tax immunity," a most esoteric of constitutional philosophies. As the Supreme Court points out in its detailed opinion, the direction taken by the clearly established law of intergovernmental tax immunity, from *McCulloch v. Maryland* to *Davis v. Michigan*, has hardly been a straight line. *See Davis v. Michigan, supra*; *Davis v. Michigan*, 109 S.Ct. 1509 (Stevens, J., dissenting). *See also Graves v. New York ex rel. O'Keefe*, 306 U.S. 466, 59 S.Ct. 595, 83 L.Ed. 927 (1939); *Helvering v. Gerhardt*, 304 U.S. 405, 58 S.Ct. 969, 82 L.Ed. 1427 (1938).

Justice Stevens, in a strongly worded dissent in *Davis*, expressed the following opinion. "Once one understands the underlying reason for the *McCulloch* holding, it is plain that this tax [Michigan's income tax] does not unconstitutionally discriminate against federal employees." *Davis*, 109 S.Ct. at 1511 (Stevens, J., dissenting).

If justices of the United States Supreme Court cannot agree that the right defined in *Davis* was clearly established before *Davis*, it hardly seems appropriate to charge the individual Defendants in this case with such perspicacity.

By virtue of the foregoing, the Court holds that the right which the Plaintiffs claim the individual Defendants violated was not clearly established before *Davis* was decided. As Justice Powell observed, in his dissent in *Owen v. City of Independence*, 445 U.S. 622, 100 S.Ct. 1398, 63 L.Ed.2d 673 (1980) (Powell, J., dissenting): "Constitutional law is what the courts say it is." Until the *Davis* decision, the courts had not said what the law was with respect to income tax schemes such as those in place in Michigan and Arizona.

The Need to Exhaust Administrative Remedies —

Defendants urge that Plaintiffs' claim for a refund should be dismissed, as the Plaintiffs did not exhaust

administrative remedies before filing suit. In their memoranda, Defendants cite A.R.S. § 42-129 as providing the only authority under which the Plaintiffs could claim a tax refund. A.R.S. § 42-129 authorizes refunds where the Department determines there has been an amount of tax paid in excess of the amount due. A.R.S. § 42-129 (D) provides that a claim for refund "be in writing and shall state the specific grounds on which it is founded." The Court is of the view that such generic language is insufficient to insure a remedy if the Plaintiffs' claims are well founded.

Defendants argue that the only avenue of relief open to Plaintiffs was to have filed a claim for refund with the Department pursuant to A.R.S. § 42-129. Furthermore, if such a claim were to be rejected, Plaintiffs would have to exhaust their appeal rights before the State Board of Tax Appeals before coming to the Tax Court.

Defendants cite numerous Arizona cases which stand for the proposition that a party must exhaust administrative remedies before he or she can come to Superior Court.

The Court's review of these authorities, however, reveals that the proposition upon which the Defendants rely is subject to numerous qualifications and exceptions. In the first place, the issue which the claimant brings to the court must have first been cognizable on the administrative level. *Minor v. Cochise County*, 125 Ariz. 170, 608 P.2d 309 (1980).

Here the issue which gives rise to the Plaintiffs' claim is whether a taxing statute is constitutional, an issue which cannot be resolved on the administrative level. An administrative body has no power to determine whether a statute compiles with a constitution. *Manning v. Reilly*, 2 Ariz. App. 310, 408 P.2d 414 (1965); *Prisk v. City of Poulsbo*, 46 Wash. App. 793, 732 P.2d 1013 (App. 1987); *Belco Petroleum Corp. v. State Bd. of Equalization*, 587 P.2d 204 (Wyo. 1978).

Furthermore, exhaustion of administration remedies is not necessary if the administrative process prescribed would not provide an adequate remedy. *Town of Paradise Valley v. Gulf Leisure Corp.*, 27 Ariz. App. 600, 557 P.2d 532 (App. 1976).

Plaintiffs' claim is premised upon the United States Supreme Court decision in *Davis,* announced some five weeks before this suit was filed. The Defendants have not made any showing that, at the time the complaint was filed, the Department had in place an administrative process which would provide the relief Plaintiffs are seeking. Indeed, the only evidence on the point, proffered by the Plaintiffs, reflects just the opposite. The public comment on the *Davis* decision by the Department was that the Department would await a judicial determination before it would recognize any claim based on *Davis.*

For the foregoing reasons, the Court holds that the Plaintiffs need not have sought relief from the Department or from the State Board of Tax Appeals before coming to the Superior Court.

The Plaintiffs' Claim for Injunctive Relief

In their complaint, Plaintiffs seek to have the Court enjoin Defendants from further enforcement of the Arizona law which imposed an income tax on their federal pensions. Since the Arizona legislature has repealed what was A.R.S. § 43-1022(A)(3), enforcement of the offending tax scheme for tax years beyond 1988 is no longer a duty imposed on the Department. Therefore, there is no need for an injunction to proscribe conduct with respect to tax years beyond 1988.

Plaintiffs also seek to have the Court enjoin further collection of taxes due but not paid by federal retirees for years prior to 1989. It is not clear to the Court whether Plaintiffs seek to enjoin collection of all delinquent income taxes or just that portion of the taxpayer's

supposed liability which is attributable to his or her federal pension.

It does not matter. Plaintiffs predicate their claim for all relief, including injunctive relief, on an assumption that there is no Arizona income tax liability on their pension income. This Court does not so find. In order for the Court to enjoin the Department of Revenue as Plaintiffs urge, the Court must find that, without such an injunction, Plaintiffs, or members of their class, will suffer irreparable harm. *Weinberger v. Romero-Barcelo*, 456 U.S. 305, 102 S.Ct. 1798, 72 L.Ed.2d 91 (1982); *Quechan Tribe of Indians v. Rowe*, 531 F.2d 408 (9th Cir. 1976); *Calvary Baptist Church at Tyler v. Adams*, 570 S.W.2d 469 (Tex. Civ. App. 1978); *Pearson v. Baldwin*, 125 Cal. App. 2d 670, 270 P.2d 866 (1954).

This Court has determined as excessive only a small portion of the income tax assessed an individual federal retiree in recent years. A taxpayer who, as a result of the Department's continuing collection effort, pays a tax that is later determined to be illegal as a result of the decision in *Davis* may have it refunded with interest. Suspending, or otherwise inhibiting, the Department's tax collection effort against all federal retirees would result in little ultimate benefit to the federal retiree taxpayer, even if preventing some illegal tax collection was the result. On the other hand, a serious disruption in the conduct of the Department's business could occur. This would be to the detriment of, not only the Department, but all non-federal retiree taxpayers in the State.

In summary, the Court finds that, if the injunction is not issued, the putative class members will suffer no irreparable harm. Therefore the Court declines to order injunctive relief.

Class Certification

Plaintiffs seek to have the Court certify a Plaintiff class, pursuant to Rule 23 of the Arizona Rules of Civil Proce-

dure. Applying the rule to the facts and issues in this case, it provides that the Plaintiffs may sue the Department of Revenue as representatives of a class of taxpayers similarly situated to themselves, "only" if:

(1) the class is so numerous that joinder of all members is impracticable,

(2) there are questions of law or fact common to the class,

(3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and

(4) the representative parties will fairly and adequately protect the interests of the class.

In order for the suit to be maintained as a class action, in addition to all of the foregoing, one of the following must also exist:

(A) The prosecution of separate actions by individual members of the class would create a risk of inconsistent adjudications which would establish incompatible standards of conduct for the Department.

(B) The prosecution of separate actions by individual members of the class would create a risk of individual adjudications which would adversely affect the interests of other members of the class who are not parties to the adjudication.

(C) The Department has acted or refused to act on grounds generally applicable to the proposed class thus making appropriate injunctive or declaratory relief with respect to the Plaintiff class.

(D) The Court finds that the questions of law and fact common to the class as a whole predomi-

> nate over questions affecting only individual members, and, that a class action is superior to other available methods for adjudicating the controversy.

Rule 23 further provides that, as soon as practicable after the commencement of an action brought as a class action, the court shall determine by order whether it is to be maintained as a class action. It is the determination of this Court that this action shall not be maintained as a class action.

There appears to be no dispute but that qualifications 1 and 2, as identified above, exist. The existence of qualifications 3 and 4 is temporized by the fact that the Plaintiffs' claim to represent two groups of class members whose interests are not identical. Indeed, their interests may well be in conflict. The impact of the offending tax scheme did not fall the same on federal civil service retirees as it did on those receiving other federal pensions.

Even so, the Court is not prepared to say that a class action could not be maintained because of a lack of typicality, or because of inadequate representation. Such a determination would necessarily await further evidence.

The issue is academic, however. The Court finds that none of the qualifications identified as A through D, above, exist in this case.

Whether a suit should be allowed to proceed as a class action is within the discretion of the court. *Godbey v. Roosevelt School Dist. No. 66*, 131 Ariz. 13, 638 P.2d 235 (App. 1981). If the court determines that the qualifications set forth in the rule for such an action do not exist, certification of a class should be denied. *Lewis v. Heckler*, 752 F.2d 555 (11th Cir. 1985).

Without the time and expense of a class action, this Court has, in this decision, made a declaration of Plaintiffs' rights as such rights are affected by *Davis v. Michi-*

gan. This declaration is made pursuant to the Arizona Uniform Declaratory Judgment Act, A.R.S. § 12-1831 *et seq*. A.R.S. § 12-1841 provides that "no declaration shall prejudice the rights of persons not parties to the proceeding."

The Court holds that, if, as a result of this lawsuit, the Department were to grant relief to a Plaintiff herein, and to deny similar relief to another taxpayer similarly situated, such disparate treatment of members of the same class would be an unlawful discrimination and would prejudice the rights of the non-Plaintiff taxpayer. Therefore, if the Plaintiffs prevail, in order to comply with A.R.S. § 12-1841, the Department must treat all taxpayers in the situation of the Plaintiffs just as they treat the Plaintiffs.

In opposing certificaiton of the Plaintiff class, the Department argued that a class action was unnecessary, as the doctrine of virtual representation would require the Department to treat all federal pensioners the same as this Court's judgment herein would require the Department to treat the Plaintiffs. Even setting aside the issue of the applicability of virtual representation, the Department, through its attorneys, represented that it would consider relevant final orders of this Court in this lawsuit just as applicable to members of the purported Plaintiff class, as to the named Plaintiffs themselves. The Court holds the Department bound by its representation.

The doctrine of virtual representation provides that a judgment or decree may adjudicate the rights of a person not a party to the adjudication, if the absent party is so well represented by a party who is before the court, that the interests of the asbent party receive actual and efficient representation. The doctrine rests on considerations of necessity, convenience, and efficiency in the administration of justice. 30A C.J.S. Equity § 145 (1965) *et seq*.; *Hale v. Hale*, 33 N.E. 858, 146 Ill. 247 (1893); *Wiley v. Schorr*, 594 S.W.2d 484 (Tex. Civ. App. 1979).

Its application is within the discretion of the court. *Noble v. Gadsden Land & Improvement Co.*, 133 Ala. 250, 31 So. 856 (1902).

The doctrine of virtual representation is a slightly redesignated descendant of a long established rule of equity known as the doctrine of representation. The definitions of the doctrines of representation and virtual representation are the same. The historical root of a court's jurisdiction to administer class actions lies in the doctrine of representation. 30A C.J.S. Equity § 145 (1965); *Hale*, 33 N.E. at 868; *Hansberry v. Lee*, 311 U.S. 32, 61 S.Ct. 115, 85 L.Ed. 22, (1940); *Covert v. Nashville, C. & St. L. Ry.*, 186 Tenn. 142, 208 S.W.2d 1008, (1948); *Simpson v. Mulle*, 358 Mich. 441, 100 N.W.2d 490 (1960). *See also Ross v. Arkansas Communities, Inc.*, 258 Ark. 925, 529 S.W.2d 876 (1975).

Virtual-representation arises from the circumstances of the litigation itself. It does not depend on the formal creation of a class. While a class action may proceed within the scope of the doctrine, representation in a class action is created by the court during the progress of the litigation.

Representation through a class action provides certain advantages. Notice of the representation is given to all prospective class members before litigation of the issues commences, and the scope of the liability of the party opposing the class is specifically defined.

The administration of class actions, however, is very expensive. The time which passes from complaint to final order in such actions tends to be much longer than in cases which are not class actions. Class actions also consume more judicial resources than other kinds of civil cases, resources which would otherwise be available elsewhere.

If the standard of efficient representation is maintained, non-parties represented by virtual representation

without a class action have the advantage of having their rights determined by a less expensive, more expedient proceeding than a class action.

Arizona recognizes the doctrine of virtual representation without a class action. *El Paso Nat. Gas Co. v. State*, 123 Ariz. 219, 599 P.2d 175 (1979). In order to insure that the standard of efficient representation is maintained, application of the doctrine by a court demands the utmost caution. *Id.* at 222, 599 P.2d at 178.

The doctrine is most commonly found in litigation in which one of the parties is a government entity, and the other party or parties are persons subject to the authority of the government party. The issue which the Court is asked to determine is whether the government party has encroached upon a right or interest of the non-government party. In all cases, the non-government party shares with numerous non-parties the same relationship with the government party. *Gist v. Stamford Hospital Dist.*, 557 S.W.2d 556 (Tex. Civ. App. 1977); *Siebert v. City of Columbia*, 461 S.W.2d 808 (Mo. banc 1970), *Williams v. Board of Sup'rs of DeSoto County*, 139 Miss. 78, 103 So. 812 (1925).

As the Arizona Supreme Court said in *El Paso Nat. Gas Co. v. State*, "This general principle has been applied to litigation instituted by a taxpayer to determine a public right or matter of public interest so that any judgment rendered therein would bind all other taxpayers." *Id.* at 222, 599 P.2d at 178.

The Mississippi Supreme Court defined the doctrine as follows:

> Actions of this character are governed by the principle that a taxpayer's suit against the governing board of a county or municipality involving questions of general interest to taxpayers prosecuted in good faith are binding upon all taxpayers as fully as

> if they had been made actual parties to the proceeding.

Williams, 139 Miss. at ——, 103 So. at 812.

This Court sees no distinction between the state as a party, and a county or municipality. Nor does it see any reason to distinguish between taxpayers subject to income tax rather than a property tax.

In this case, identifying the members of the purported class is peculiarly within the resources of the Defendant Department of Revenue. The posture of this litigation is such that no affirmative relief can be obtained against the non-party class members, even for the costs of litigation. The Defendant does not resist application of the doctrine, and the Court has jurisdiction to order relief for the entire class, not just the named Plaintiffs. Most important of all, Plaintiffs have thoroughly, even exhaustively, presented to the Court the position of the taxpayer class on what *Davis v. Michigan* requires of Arizona.

The Court holds that, in the absence of a fact or circumstance which affects the representative capacity of the named taxpayer, where a taxpayer, pursuant to an application for declaratory relief, obtains a judgment, decree, or order against a taxing authority, such judgment, decree, or order, or the benefits thereof, applies to all other taxpayers, similarly situated to the complaining taxpayer, the same as to the taxpayer who made the application.

Pursuant to the foregoing, the Court directs the Department of Revenue to treat all federal retirees who have paid Arizona income taxes within the applicable time period as though they were named Plaintiffs herein.

The Court, having taken the stand set forth above, and considering the qualifications identified as A through D above, finds that none of such qualifications for a class action exist.

Notice to Affected Taxpayers

Immediately upon the judgment herein becoming final, the Department is to create such forms as it feels to be expedient to effect the refund ordered herein. Once such forms are created, the Department is to mail them, along with adequate instructions, to all persons who have paid income tax to the State of Arizona on income which includes federal pension income paid to the retirees during any tax year from 1984 through 1988, inclusive.

In addition, the Department is to publicize the entitlement to refund in all media which it calculates may reach the attention of any person to whom to such a refund may be due. The media to which the Department circulates information is to be that which the Department deems to be adequate to reach all of the affected class, but not less than as described by the Departments' attorneys on page 5 of its memorandum filed October 13, 1989, captioned, "Submission of Defendant Departments' Plan to Implement Final Judgment Without Class Certification."

Theory of Remedy

The Plaintiffs argue that the remedy mandated to this Court by the *Davis* decision is a refund, plus applicable interest, of all taxes paid Arizona by federal pensioners, to the extent such taxes were paid from the pensioner's pension.

The Plaintiffs cite to the Court *Hackman v. Director of Revenue*, 771 S.W.2d 79 (Mo. banc 1989), decided by the Supreme Court of Missouri on May 25, 1989. *Hackman* is to Missouri as *Bohn* is to Arizona. Missouri in *Hackman*, like Arizona in *Bohn*, was faced with reconciling *Davis v. Michigan* with the State's discriminatory tax scheme. It was the decision of the *Hackman* court to refund to Hackman (only) all the roughly $2,300 he claimed as a refund. In doing so, the Missouri court acknowledged that it was establishing a precedent that

would likely provide full refunds for those taxpayers who could establish their claims pursuant to Missouri law. 771 S.W.2d at 82.

This Court is not persuaded by the decision in *Hackman*. *Hackman* holds that Missouri law requires that an overpayment of taxes be refunded and that "an overpayment includes those income taxes collected illegally under a taxation scheme which violates principles of intergovernmental tax immunity". 771 S.W.2d at 81.

It is not clear from the *Hackman* opinion why the Missouri court found that all of the taxes collected from federal retirees were illegally collected. In *Hackman*, it appears that the only issue considered by the court was whether *Davis* should apply prospectively or retrospectively. With Missouri, it was all or none.

The Department argues that the cost to Arizona of such a refund as the Plaintiffs seek would be 261 million dollars, an amount so large that it would endanger the financial integrity of the state. Department of Revenue, Second Supplemental Statement of Facts, filed August 29, 1989. Combined with the other circumstances present in this case, applicable law permits the Court to order no retrospective remedy at all. The Department urges the Court to so hold.

Where a violation of law results in economic loss, that a successful Plaintiff should recover that economic loss is a fundamental proposition of the law of civil remedies. That the violation of law is also a violation of the federal Constitution does not diminish the validity of the basic proposition, although state law may affect its implementation. Furthermore, there are situations where the impact of an unforeseen interpretation of the federal Constitution is so significant that a state is permitted to apply its remedy prospectively only. *Chevron Oil Co. v. Huson*, 404 U.S. 97, 92 S.Ct. 349, 30 L.Ed.2d 296 (1971); *Cipriano v. City of Houma*, 395 U.S. 701, 89 S.Ct. 1987, 23

L.Ed.2d 647 (1969); *National Can Corp. v. Department of Revenue*, 109 Wash.2d 878, 749 P.2d 1286 (1988).

The leading authority on when a state may apply, prospectively only, a remedy for a violation of the Constitution is *Chevron Oil Co. v. Huson, supra. Huson* provides for a three prong test. Applying the three prongs of *Huson* to the case before the bench, in order for the Court to rule in the Department's favor, the Court must find: (1) that *Davis v. Michigan* established a new principle of law; (2) that denial of retrospective relief would not seriously offend principles of intergovernmental tax immunity; and (3) that granting retrospective relief creates such serious inequity that such inequity outweighs the equity of appropriate redress for those injured by the constitutional violation.

For reasons set forth herein in the discussion on the Plaintiffs' § 1983 claims, this Court finds that the first prong of *Huson* has been satisfied. The Court, however, does not find that there is any serious inequity in a refund to Plaintiffs that reimburses them for the economic loss incurred as a result of the constitutional violation.

The Plaintiffs, however, seek much more than their economic loss.

The Plaintiffs' claim that any tax at all on their pensions was an illegal tax, and therefore they are entitled to a full refund. *Davis* did not so hold. The Plaintiff in *Davis* was not identified as a representative of a class. The Supreme Court opinion in *Davis* does not specifically define the extent of the refund sought by *Davis*. The Court concluded that the Michigan Income Tax Act violated principles of intergovernmental tax immunity because it favored retired state government employees over retired federal employees. Michigan had already conceded that, if the Court so held, a refund was appropriate. Based solely on this concession, the Court ruled Davis entitled to a refund. *Davis*, 109 S.Ct. at 1508-09.

Davis held that the constitutional right the Michigan tax system violated was a right inuring to the United States, not an individual right guaranteed to the Plaintiff. *Davis*, 109 S.Ct. at 1507; *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) at 436.

This is not to say that the Plaintiffs have no claim. *Davis* makes it clear that they do. *Davis, supra.* But it is not, however, a claim based on a violation of an individual fundamental right.

Plaintiffs' claim to a full refund is premised on the general proposition that legislation determined to be unconstitutional is void. This argument misses the point. "If part of an act is unconstitutional, but by eliminating the unconstitutional portion the balance of the act is workable, only that part which is objectionable will be eliminated and the balance will be left intact." *State v. Jones,* 142 Ariz. 302, 306, 689 P.2d 561, 565 (1984).

The legislation which imposed an income tax on the Plaintiffs' pensions was the same legislation that imposed an income tax on income accrued during the taxable year by taxpayers in general. Would the Plaintiffs have the Court declare the entire State income tax law void? *Davis* makes it clear that such drastic action is not required. "While invalidation of Michigan's income tax law in its entirety obviously would eliminate the constitutional violation, the Constitution does not require such a drastic solution." *Davis v. Michigan,* 109 S.Ct. at 1509.

If the Court must focus on specific legislation to invalidate, it would have to be the two exemptions provided in A.R.S. § 43-1022(3) and A.R.S. § 43-1022(4).

In their demand for a full refund, the Plaintiffs ignore what *Davis* teaches. Even with the concession by Michigan, the award of the court was qualified. According to the Court, Davis was entitled to a refund "to the extent . . . [he] paid taxes pursuant to this invalid scheme." *Davis,* 109 S.Ct. at 1508-09.

Earlier in its opinion, the Supreme Court interpreted § 111 to waive any immunity enjoyed by federal employees from state taxation of their incomes "except to the extent that such taxation discriminates on account of the source of the compensation." *Id.* at 1505.

The doctrine of intergovernmental tax immunity does not preclude a state from taxing income from federal compensation. *Graves, supra.* It does preclude discriminatory taxation. It is the discrimination and not the taxation which must be remedied.

There are two elements for determining whether taxing legislation violates the doctrine of intergovernmental tax immunity. The state must seek to impose an income tax on compensation from a federal source, and it must impose a lesser tax on compensation from a state source. Both elements must be present. It is only when the two elements combine that the fatal discrimination occurs.

An argument can fairly be made that such discrimination as is defined herein is the rule rather than the exception in income tax legislation. Rates discriminate which increase as income increases. Within recent memory, the federal income tax has discriminated as between the old and the not so old, the blind and those who see, those who have and those who don't, the sick and the well, the benevolent and the stingy, and those with families and those without. The foregoing list is not exhaustive. Discrimination of this sort has been upheld in the courts if it represents a rational means of achieving a legitimate governmental interest. In most such cases, such discrimination comes about because of a legislative intent to confer a benefit, not to impose a penalty.

In the present case, the Arizona legislature intended to confer a benefit on state pensioners and on federal civil service retirees. It did not identify non-civil service federal retirees in a separate tax class. The tax cost of the benefits conferred on state pensioners and retired federal civil servants fell upon all non-benefiting taxpayers. The

discrimination about which Plaintiffs lament with such fervor fell just as hard on every taxpayer not receiving a state or civil service pension as it fell upon the federal retiree.

A government collects in taxes what it decides it needs to bear the cost of government. If a class of taxpayers receives the benefit of a lowered tax, all other taxpayers incur a relative increase. If the Court were to order the refund which the Plaintiffs claim, such an order would be tantamount to excusing federal retirees from state income tax liability on their pensions. This Court, indeed no court, can confer such a magnanimous benefit. If federal retirees are to receive such treatment, it must be authorized by the legislature. *Apache County v. Atchison, Topeka & Santa Fe Ry.*, 106 Ariz. 356, 476 P.2d 657 (1970).

If a constitution requires it, a court may invalidate legislation, but it may not substitute its own scheme for that invalidated. Here, the legislation which created the discrimination which *Davis* found unconstitutional was that which exempted from taxation state pensions and part of civil service pensions. It is to the impact of these exemptions on the class against whom *Davis* held the discrimination fell, that the Court must look for a remedy.

There is guidance for the Court in the *Davis* opinion. Intergovernmental tax immunity does not prohibit the whole tax but "the extent that such taxation discriminates." The Court holds that the measure of the extent that the exemptions set forth in A.R.S. § 43-1022(3) and A.R.S. § 43-1022(4) discriminated against federal retirees is the amount of tax such retirees paid that is greater than they would have had to pay if the provisions which created the discrimination had not been in place. *Bade v. Drachman*, 4 Ariz. App. 55, 64, 417 P.2d 689, 697 (1966).

If a taxpayer seeks a refund of taxes reflected on an unchallenged return, such refund must be claimed within

four years after the return was required to be filed. A.R.S. § 42-115. The *Davis* decision was announced on March 28, 1989. This lawsuit was filed May 1, 1989. The Court holds that, because of the doctrine of virtual representation, limitations tolled by the filing of the complaint herein are tolled for all taxpayers similarly situated to Plaintiffs, not just the named Plaintiffs themselves.

The income tax for 1984 was due on April 15, 1985. An alert, or alerted, taxpayer might have filed a claim for a refund based on *Davis* before April 15, 1989. Many taxpayers may have obtained extensions in 1985 which did not make their returns due until after May 1, 1985. *Davis* mandates that all affected taxpayers receive equal treatment. The Court concludes that it would be less than equal treatment to favor taxpayers because they reacted quickly to the *Davis* decision, or because they obtained an extension five years earlier for reasons not related to *Davis*. The Court holds that all affected taxpayers are entitled to refunds for all tax years, 1984 through 1988.

The Court also has some concern that statutory limitations on some of the relevant tax years will be upon us before the decision herein becomes final, and before all affected taxpayers have been informed of their rights hereunder. The Court therefore holds that claims authorized herein may be filed until the first April 15 two years after this decision becomes final or until the expiration of the limitations set forth in A.R.S. § 42-115, whichever is later.

Computation of the Remedy

It is now the Court's task to convert the abstract standard announced above into a formula which the Department can apply to effect the relief directed. In doing so, the Court is limited to the facts supplied by the Department. There are less of these than the Court would have liked. As a result, approximation must, to some extent, replace precision. In the course of this litigation, after this Court announced its decision in principal, the

Department was charged with supplying the Court with sufficient data to permit the Court to fashion its remedy. In the main, the Department complied. In some respects, however, the data supplied supported only the Department's theory of an appropriate refund and did not reach that decided by the Court.

The Court, therefore, took judicial notice of some facts not supplied. When the information available to the Court was not sufficiently detailed to be exact and was a necessary element of the computation, the Court applied the data most beneficial to the Plaintiffs. The Court has also determined that further delay to obtain more precise information would be of no benefit to either party. Also, in making its determination herein, the Court has placed a value on simplicity.

Despite all of the foregoing, the Court, after exhaustive review of the data provided, is satisfied that, whatever lack of precision there may be in the Court's formula, it is minimal, and of insignificant consequence.

Most of the data utilized by the Court can be found in the exhibits attached to a document filed by the Department on October 13, 1989. The Document is entitled "Defendants' Opposition to Reconsideration of Refund Ruling and Submission of Refund Plan."

The Court assumes that revenue received by the State from individual income taxes for any year is all of the revenue that is required by the State from such a source for that year. Therefore, if state pensioners had paid income tax on their state pensions and civil service retirees had paid income tax on all of their pensions, all other taxpayers, including the Plaintiffs, would have paid less income tax. The difference between what they paid and what they would have paid is the measure of the refund to which federal retirees are entitled.

Mathematically, the proportionate tax reduction can be defined as a fraction, the numerator of which is the addi-

tional tax that would have been collected if no exemptions had been allowed, and the denominator of which is the numerator plus the total tax collected from individuals. Calculations which support the Court's narrative herein are set forth in Appendix A attached to this decision.

The Department has provided the Court with the amount of income tax obtained from individuals for each of the relevant tax years. This is an element of the denominator.

The Department has also provided the Court with the number of civil service retirees resident in Arizona for each relevant tax year. It has not provided any information which would permit the Court to ascertain how many such retirees failed to utilize the full exemption to which they were allowed. In computing the civil service element of both the numerator and the denominator, the Court has assumed that all civil service retirees utilized the full exemption authorized by A.R.S. § 43-1022(4). The civil service element is calculated by multiplying the number of civil service retirees times 200 (.08 times 2,500).

The Department has provided the Court with the total amount of Arizona pensions paid for each of the relevant years. It has not provided the Court with any data that any such income without the exemption would not have been subject to Arizona income tax.

The Department has identified an effective tax rate of 5.6%, but it has not provided the Court with a definition of "effective tax rate." From the information supplied, the Court cannot discern if the effective tax rate is the average rate for all taxpayers for all income or is the average effective rate for pension income.

If Arizona pensioners had been required to pay tax on their pension income, the pension income would have been added to their other income and would have been effectively taxed at the taxpayer's highest rate. An average effective tax rate for total income is of little value in

attempting to discern an effective tax rate for less than total income. When total income is taxed at graduated rates which increase as income rises, tax on both additions and subtractions to income should be computed at top rates, not average rates. The Court has computed the Arizona pension element of the numerator and the denominator by multiplying total Arizona pension income by eight percent, the top Arizona rate for all relevant years.

In reducing the thus computed fraction to a proportion for each of the relevant tax years, the Court finds there is very little difference between years in the computed percentage. It varies between a low of .02596 in 1984, and .02810 in 1988. When this difference is translated into a tax refund, it reflects a very small sum of money.

The Court finds that the administrative benefit of using a single constant for all relevant years outweighs the slight cost of more precision to an individual taxpayer whose pension might be at the high end. The Court, therefore, finds an effective hypothetical tax reduction for all years to be 2.75%.

There are two more adjustments to consider. The data available to both the individual taxpayer and the Department is not the tax paid on pension income but the amount of pension income, included in Arizona gross income, or subject to the civil service exemption. From such income data must be determined the tax paid on included pension income.

Once again, the value of simplicity in administration is considered. For purposes of the computation herein, the tax paid on the taxpayer's pension income is computed by multiplying the total pension income included in gross income, or subject to the civil service exemption, times the highest Arizona rate paid by the taxpayer for the computation year.

For all but civil service pensions, the refund to which the taxpayer is entitled is determined by multiplying the thus computed tax paid on the federal pension by .0275.

Civil service pensioners, however, to the extent they were able to take advantage of the civil service exemption, paid less than they would have had to pay had the unlawful exemptions not been in place. Therefore, in order to put civil service pensioners on the same footing as other federal pensioners, the civil service refund has to be adjusted by subtracting the amount of the tax benefit already received.

For civil service retirees, therefore, after computing the refund as above, an amount equal to the taxpayers top rate times the amount of the exemption utilized must be subtracted. The resulting figure is the refund to which the civil service retiree is entitled.

No refund can be greater than the tax paid.

To any refund paid, the Department is to add interest at rates the Department pays on income tax refunds. The interest is to be computed from the date the tax return on which the tax was paid was due, until the refund is paid to the taxpayer.

/s/ William T. Moroney
WILLIAM T. MORONEY
Judge of the Arizona Tax Court

This Opinion Filed: April 6, 1990

Appendix A

Calculation of Refund Factors

For each tax year, State retirees were allowed a 100% deduction on their retired pay. Federal civil service retirees were allowed a $2500 deduction. All other federal retirees were allowed no deduction.

The value of the State and federal civil service deductions is calculated based on the top Arizona tax rate of 8%. The value in uncollected tax of a $2500 subtraction from income would thus be $200.00. The value in uncollected taxes of the 100% state retiree subtraction is calculated by multiplying gross state pensions for each year times 8%. Each of these figures constitutes the hypothetical revenue the State would have collected had the exemption scheme not existed.

For each tax year, the refund factor requires the number of federal civil service retirees, the gross pensions paid for state retirees, and the actual revenue collected by Arizona on personal income taxes. The tax rate for all calculations is 8%.

All figures are derived from Department of Revenue Annual Reports for the subject years, and from the briefs of the parties.

1984:

Arizona Revenue Collected: $626,244,000.00
# of federal civil service retirees: 32,805
Gross State pensions: $126,620,000.00
State hypothetical revenue: $126,620,000.00 × .08 = $10,129,600.00
Federal Civil Service hypothetical: 32,805 × $200.00 = $6,561,000.00

$$\text{Calculation: } \frac{6{,}561{,}000 + 10{,}129{,}600}{626{,}244{,}000 + 6{,}561{,}000 + 10{,}129{,}600} = .02596002$$

1985:

Arizona Revenue Collected: $702,957,000.00
# of federal civil service retirees: 33,851
Gross State pensions: $156,228,000.00
State hypothetical revenue: $156,228,000.00 × .08 = $12,498,240.00
Federal Civil Service hypothetical: 33,851 × $200.00 = $6,770,200.00

$$\text{Calculation: } \frac{6{,}770{,}200 + 12{,}498{,}240}{702{,}957{,}000 + 6{,}770{,}200 + 12{,}498{,}240} = .02667925$$

1986:

Arizona Revenue Collected: $761,422,000.00
# of federal civil service retirees: 35,169
Gross State pensions: $180,983,000.00
State hypothetical revenue: $180,983,000.00 × .08 = $14,478,640.00
Federal Civil Service hypothetical: 35,169 × $200.00 = $7,033,800.00

$$\text{Calculation: } \frac{7{,}033{,}800 + 14{,}478{,}640}{761{,}422{,}000 + 7{,}033{,}800 + 14{,}478{,}640} = .027476681$$

1987:

Arizona Revenue Collected: $853,980,000.00
# of federal civil service retirees: 36,194
Gross State pensions: $204,051,000.00
State hypothetical revenue: $204,051,000.00 × .08 = $16,324,080.00
Federal Civil Service hypothetical: 36,194 × $200.00 = $7,238,800.00

$$\text{Calculation: } \frac{7{,}238{,}800 + 16{,}324{,}080}{853{,}980{,}000 + 7{,}238{,}800 + 16{,}324{,}080} = .026850972$$

1988:

Arizona Revenue Collected: $911,618,000.00
# of federal civil service retirees: 37,497
Gross State pensions: $235,715,000.00
State hypothetical revenue: $235,715,000.00 × .08 = $18,857,200.00
Federal Civil Service hypothetical: 37,497 × $200.00 = $7,499,400.00

$$\text{Calculation: } \frac{7{,}499{,}400 + 18{,}857{,}200}{911{,}618{,}000 + 7{,}499{,}400 + 18{,}857{,}200} = .02809948$$

The average of all the refund ratios is .0270132.
The Court has, for the sake of simplicity, applied an overall ratio of .0275.

APPENDIX D

THE SUPERIOR COURT
OF THE STATE OF ARIZONA
IN THE ARIZONA TAX COURT

No. TX 89-00050

JOHN L. BOHN, *et al.*

v.

PAUL WADDELL, *et al.*

SUPPLEMENTAL OPINION

MORONEY, Judge

On April 6, 1990, this Court, pursuant to A.R.S. § 12-171, issued its Opinion on certain issues presented to the Court by the litigants. Among other things, the Court decided that "the scheme for taxing state and federal pensions, as existed before the recent amendment to A.R.S. § 43-1022, was in violation of federal law, and further, was in violation of the federal constitutional doctrine of intergovernmental tax immunity." *Bohn v. Waddell*, 164 Ariz. 74, 80, 790 P.2d 772, 778 (Tax 1990). The Court also held that the Taxpayers' remedy for the constitutional violation was a refund of the excess tax paid by the Taxpayers because of the discriminatory scheme.

After the foregoing Opinion was pubilshed, the U. S. Supreme Court announced decisions in four cases, all of which involved state tax issues. The four cases were *McKesson Corp. v. Florida Div. of Alcohol & Tobacco*, 495 U.S. ——, 110 S.Ct. 2238, 110 L.Ed.2d 17 (1990);

American Trucking Ass'ns, Inc. v. Smith, 495 U.S. ——, 110 S.Ct. 2323, 110 L.Ed.2d 148 (1990) (plurality opinion); *Ashland Oil, Inc. v. Caryl*, 495 U.S. ——, 110 S.Ct. 3202, 110 L.Ed.2d 734 (1990) (per curiam); and *National Mines Corp. v. Caryl*, 495 U.S. ——, 110 S.Ct. 3205, 110 L.Ed.2d 740 (1990) (per curiam). Hereafter, the Court will refer to the four cases as *McKesson*, *Smith*, *Ashland Oil*, or *National Mines*.

On the strength of law announced in these four U. S. Supreme Court cases, the Taxpayers made a motion that the Court withdraw its Opinion from publication and reconsider its ruling that the Taxpayers were entitled to less than a full refund of all taxes paid on their federal pensions. The Court agreed to reconsider its decision and invited further briefing from the litigants. The sole decision presented to the Court for reconsideration was whether or not the Taxpayers should receive a full refund of all taxes paid on their federal pensions.

The Court has reconsidered its earlier decision in light of the four U. S. Supreme Court cases cited. The Court denies the relief requested by the Taxpayers. The Court finds no authority in any of the four cases for the position urged by the Taxpayers. The Court further affirms the decisions made previously and announced in its Opinion of Apri 16, 1990.

In this Opinion the Court seeks not only to review the application to the case before the bench of the four U. S. Supreme Court opinions cited, but also to clarify the Court's rationale in reaching the decision it has reached with respect to the Taxpayers' remedy.

All of the U. S. Supreme Court cases cited concern state taxes which the Supreme Court, either in the subject case or in an earlier one, had ruled violated the commerce clause of the federal constitution. *McKesson* was concerned with what a state owed to a taxpayer discriminated against by a state law determined to be unconstitutional.

The other three cases concerned the non-retroactive application of a Supreme Court decision overturning a state tax.

McKesson involved a Florida liquor excise tax which provided for rate reductions for liquor manufactured from agricultural products commonly grown in Florida, and used in alcoholic beverages produced in Florida. McKesson was a producer of alcoholic beverages manufactured from products not commonly grown in Florida, and therefore, did not enjoy the rate reductions granted to some of its competitors. When McKesson challenged Florida's scheme, the Florida Supreme Court held the scheme unconstitutional, but denied McKesson a refund. McKesson appealed the denial of a refund to the U. S. Supreme Court.

Florida law required a taxpayer seeking to challenge the validity of the liquor excise tax to pay the tax as assessed and effectively pursue its challenge postpayment. Florida also had in place a general statute which provided for refunds for the overpayment of any tax. This statute is the vehicle *McKesson* used to get to court. *McKesson*, 110 S.Ct. at 2243.

Justice Brennan succinctly announced the holding of the Supreme Court in the following language:

> Our precedents establish that if a State penalizes taxpayers for failure to remit their taxes in timely fashion, thus requiring them to pay first and obtain review of the tax's validity later in a refund action, the Due Process Clause requires the State to afford taxpayers a meaningful opportunity to secure postpayment relief for taxes already paid pursuant to a tax scheme ultimately found unconstitutional. We therefore agree with petitioner that the state court's decision denying such relief must be reversed.

Id. 110 S.Ct. at 2242.

Since Arizona income taxes are not required to be paid before a determination of the validity of the tax, A.R.S.

§ 42-122(A); A.R.S. § 42-124(B)(2), *McKesson* does not govern any issue presented in the case before the bench. Certain propositions announced in *McKesson*, however, are useful in analyzing the federal law which does apply.

The authorities reviewed in *McKesson* by which the court defined the taxpayers' rights, are all predicated on a coercive pre-payment. As an example, the *McKesson* Court described the holding in *Montana Nat. Bank of Billings v. Yellowstone County*, 276 U.S. 499, 48 S.Ct. 331, 72 L.Ed. 673 (1928), as follows: "One forced to pay a discriminatorily high tax in violation of federal law is entitled, in addition to prospective relief, to a refund of the excess tax paid—at least unless the disparity is removed in some other manner." *McKesson*, 110 S.Ct. at 2249.

Even though the stated proposition rests upon a predicate that does not exist in this case, this Court has no quarrel with restating the proposition: In general, one who pays a discriminatorily high tax in violation of federal law is entitled, in addition to prospective relief, to a refund of the excess tax paid—at least unless the disparity is removed in some other manner.

There are, however, exceptions to this general proposition. In an appropriate case, in deciding whether to apply the rule cited, the Court must consider all factors which affect, or may be affected by, the decision to be made. In the case at bench, such factors might include the inherent differences between an excise tax and an income tax, limitations on a court's authority, and the impact of the court's ruling on a state's overall tax scheme.

The most relevant aspect of *McKesson* is that it did not prescribe a remedy. It left it to Florida to fashion one consistent with the constitutional parameters set forth in the opinion. *McKesson*, 110 S.Ct. at 2258.

The tax involved in *Smith* was a highway use tax in Arkansas which was imposed as a flat tax. While

the Arkansas case was proceeding through the courts, the U.S. Supreme Court in *American Trucking Ass'ns, Inc. v. Scheiner*, 483 U.S. 266, 107 S.Ct. 2829, 97 L.Ed.2d 226 (1987), held that a flat highway use tax was unconstitutional as a violation of the commerce clause. The issue in *Smith* was whether or not the *Scheiner* decision would be applied retroactively in Arkansas. In *Smith*, the Supreme Court was divided in a somewhat unusual manner. Four Justices felt that, as a matter of substantive federal law. *Scheiner* should be held prospective only, and four Justices held the opposite.

Justice Scalia cast the deciding vote that *Scheiner* should not be applied retroactively. Unlike the eight other Justices, Justice Scalia felt that the Supreme Court should abandon its philosophy of negative enforcement of the commerce clause and should not hold a state statute in violation of the commerce clause unless it is in conflict with a congressional enactment. For that reason, Justice Scalia did not feel that the Arkansas tax (nor the Pennsylvania tax overturned in *Scheiner*) was a violation of the commerce clause in the first place. Because of Justice Scalia's vote, the four justices who favored non-retroactive application of *Scheiner* constitute the plurality, and the four Justices who favored retroactive application of *Scheiner* constitute the dissent.

A plurality opinion is not thought to be authoritative precedent. *Marks v. United States*, 430 U.S. 188, 193 (1976). As Justice Rehnquist observed in *Texas v. Brown*, 460 U.S. 730, 737 (1982), a four Justice plurality opinion by the Court is not a binding precedent, but "as the considered opinion of four Members of this Court it should obviously be the point of reference for further discussion of the issue." *See also United States v. Pink*, 315 U.S. 203, 216 (1941) (decision of equally divided Court not authoritative precedent). Even so, there is more grist for apposite analysis in *Smith* than in any of the other three cases.

The plurality in *Smith* cites *Chevron Oil Co. v. Huson*, 404 U.S. 97, 92 S.Ct. 349, 30 L.Ed.2d 296 (1971), as authority for its non-retroactive holding. Relying on the same authority, the Arkansas Supreme Court had previously reached the same result. *Huson* prescribes a three-prong test to determine whether the invalidation by a court of a law should apply retroactively. *Id.*, 404 U.S. at 106, 107. Under the third prong of *Huson*, the court considers the equities of retroactive application. *Smith*, 110 U.S. at 2332. *Bohn v. Waddell*, 164 Ariz. at 91, 92, 790 P.2d at 789, 790.

In discussing the third prong, the Arizona court found that a total refund would allow out-of-state truckers "an unconscionable windfall far in excess of a fair recovery for the discrimination they may have suffered due to the tax." *Smith*, 110 S.Ct. at 2329 (quoting *American Trucking Ass'n v. Gray*, 295 Ark. 43, 47, 746 S.W.2d 377, 379 (1988)). The same conclusion can be drawn in the case before the bench.

In *Smith*, the only question before the Court was whether the Arkansas court applied *Chevron* correctly. The plurality decided that it had; the dissent disagreed.

In deciding that *Scheiner* should not apply retroactively, the plurality decided that *Scheiner* overturned what had been settled case law. The plurality distinguished *McKesson* from *Scheiner* on that ground, noting that Florida should have known that its tax was unconstitutional when it enacted it. *Smith*, 110 S.Ct. at 2333; *McKesson*, 110 S.Ct. 2238 at 2255.

The plurality was motivated by its perception that retroactive application of *Scheiner* in Arkansas would be manifestly unjust. The dissent was concerned over the disparate treatment by the court in two cases with a virtually identical issue, where the second case was in the pipeline when the first case (*Scheiner*) was decided.

The dissent distinguishes between two kinds of retroactive effect. One is a rule of federal constitutional law

which is an element in the decision which the Court makes in its assessment of unconstitutionality. The other type of retroactive effect occurs by virtue of the remedy to be applied once the case is decided. *Scheiner* invalidated a Pennsylvania tax virtually identical to the Arkansas tax in *Smith*. In *Scheiner*, the court did not hold its determination to be non-retroactive. The dissent felt that fairness demanded that the same decision be made in *Smith*. The dissent would hold that every case which rules a law unconstitutional should apply retroactively to every controversy that has not been laid to rest by an applicable statute of limitations or by a final judgment. The dissent suggests that there may be relief in the law of remedies from an unfair or harsh result.

The dissent distinguishes *Huson* as a remedy case and further distinguishes it because it involves a statute of limitations, an area in which federal courts have much equitable discretion.

In *Ashland Oil*, the issue was whether *Armco, Inc. v. Hardesty*, 467 U.S. 638, 104 S.Ct. 2620, 81 L.Ed.2d 540 (1984), should be applied retroactively. The tax in this case was a West Virginia gross receipts tax which *Armco* had invalidated. In *Ashland*, the Supreme Court found that *Armco* did not establish a new principle of law. *Ashland*, 110 S.Ct. at 3205. Therefore, under the law as determined by the plurality in *Smith*, *Armco* would not apply retroactively. *Id.* The dissent in *Smith* would apply any constitutional decision retroactively to cases on direct review. *Ashland*, 110 S.Ct. 3204 (citing *Smith*, 110 S.Ct. at 2352 (Stevens, J., dissenting)). Therefore under either theory, *Armco* should apply retroactively.

National Mines involved the same tax and the same issue as *Ashland Oil*, that is, whether *Armco* should be applied retroactively. The U. S. Supreme Court, relying on its decision in *Ashland*, held that it should. *National Mines*, 110 S.Ct. at 3205.

Many issues were raised by the litigants in this case. The most significant of these issues were analyzed and decided in this Court's Opinion of April 6, 1990. The remainder, nearly as many, were resolved by minute order of the Court on April 6, 1990. The only issue in the case, however, of any real significance to the Taxpayers is the issue which the Court now has reconsidered.

Davis v. Michigan, 489 U.S. 803, 109 S.Ct. 1500, 103 L.Ed.2d 891 (1989), made the invalidation of the Arizona tax scheme a certainty. Once that low hurdle is leaped, the only decision that can benefit the Taxpayers is what relief they are to get as a result of the invalidation. The Taxpayers have argued that they are entitled to a refund of all taxes paid on their federal pensions. This Court has held otherwise, and now reaffirms its earlier decision.

The Taxpayers have never precisely explicated to the Court their argument in favor of full refunds. Nevertheless, the Court believes it can be simply stated as follows. The doctrine of intergovernmental tax immunity prohibits a discriminatory state tax on income received from the federal government. The invalidated Arizona tax scheme imposed such a tax. Therefore, the tax imposed is void and must be refunded.

The proposition that an unconstitutional act is void appears to have first been announced in the early constitutional landmark, *Marbury v. Madison*, 5 U.S. 137, 1 Cranch. 137, 2 L.Ed. 60 (1803). It was reaffirmed in *Ex Parte Siebold*, 100 U.S. 371, 10 Otto 371, 25 L.Ed. 717 (1879), and *Norton v. Shelby County*, 118 U.S. 425, 6 S.Ct. 1121, 30 L.Ed. 178 (1886).

In *Norton v. Shelby County, supra*, the rule was stated with a measure of rhetorical elegance as follows: "An unconstitutional act is not a law; it confers no rights; it imposes no duties; it affords no protection; it creates no office; it is, in legal contemplation, as inoperative as though it had never been passed." 118 U.S. at 442.

Even though federal law must be applied to decide the issue, the proposition apparently relied upon by the Taxpayers is well set forth in the state case of *Crane Co. v. Arizona Tax Comm'n*, 63 Ariz. 426, 442, 163 P.2d 656, 662 (1945). "The general rule appears to be that an unconstitutional statute is in reality no law and is wholly void, and is inoperative as if it had never been passed."

Thus set forth, the general rule is stated in uncompromising language. Constitutional law, however, is conceptual, not preceptual. In holding a law unconstitutional, the U.S. Supreme Court has often not applied the general rule. *Lemon v. Kurtzman*, 411 U.S. 192, 197-98 (1973).

In *Chicot County Drainage Dist. v. Baxter State Bank*, 308 U.S. 371, 60 S.Ct. 317, 84 L.Ed. 329 (1940), the court made the following comment:

> The courts below have proceeded on the theory that the Act of Congress, having been found to be unconstitutional, was not a law; that it was inoperative, conferring no rights and imposing no duties, and hence affording no basis for the challenged decree. *Norton v. Shelby County*, 118 U.S. 425, 442; *Chicago, I. & L. Ry. Co. v. Hackett*, 228 U.S. 559, 566. It is quite clear, however, that such broad statements as to the effect of a determination of unconstitutionality must be taken with qualifications. The actual existence of a statute, prior to such a determination, is an operative fact and may have consequences which cannot justly be ignored. The past cannot always be erased by a new judicial declaration. The effect of the subsequent ruling as to invalidity may have to be considered in various aspects,—with respect to particular relations, individual and corporate, and particular conduct, private and official. Questions of rights claimed to have

> become vested, of status, of prior determinations deemed to have finality and acted upon accordingly, of public policy in the light of the nature both of the statute and of its previous application, demand examination. These questions are among the most difficult of those which have engaged the attention of courts, state and federal, and it is manifest from numerous decisions that an all-inclusive statement of a principle of absolute retroactive invalidity cannot be justified.

308 U.S. at 374.

Arizona also has repudiated the absolutism of the general rule as expressed in *Crane*. In *Shreve v. Western Coach Corp.* 112 Ariz. 215, 216-17, 540 P.2d 687, 688-89 (1975), the court said: "Thus it was said that an unconstitutional law . . . 'is, in legal contemplation, as inoperative as though it had never been passed.' This Blackstonian view, based on the theory that judges discover, rather than make the law, has been considerably eroded with time, and is not the law in Arizona." (citations omitted). Also in *Selective Life Insurance Co. v. Equitable Life Assur. Soc.*, 101 Ariz. 594, 602, 422 P.2d 710, 718 (1967), the Court stated: "Arizona has rejected the doctrine that acts performed under an unconstitutional statute must always be invalid."

The issue of non-retroactivity as faced in three of the four U.S. Supreme Court cases under study is itself an example of the consideration which the Supreme Court must make in ruling on the effect of a determination of invalidity. As Justice O'Connor indicated in the plurality opinion in *Smith*, the determination of the effect of such a ruling requires a hard look at whether the application of the general rule would be unjust. *Smith*, 110 S.Ct. at 2332.

This Court is of the opinion that federal law requires that a court, in invalidating a law on constitutional

grounds, must weigh the effect of its retroactive application, and, if it concludes substantial inequities will result from such an application, it may hold its ruling to be non-retroactive. Even if it holds its ruling to be retroactive, it should qualify the retroactive application of its ruling if equitable considerations require that it do so.

This ruling is in accord with the three-prong approach of *Chevron Oil Co. v. Huson*, 404 U.S. at 106, since both the first and second prongs are themselves equitable considerations. This ruling is also in accord with both the plurality and the dissent in *Smith*. The Court, therefore, need not decide what the U.S. Supreme Court in *Smith* could not: whether *Huson* defines constitutional law or is a remedy case. Since Arizona income taxes were not coercively extracted as a condition of challenging the law found unconstitutional, and since this is not a commerce clause case, the Court need not attempt to fashion a remedy as dictated by *McKesson*. *Huson* is applicable if its tests are met whether it is a remedy case or not.

In determining the constitutional law effect of the invalidation of state law, federal law applies. *Smith*, 110 S.Ct. at 2330. Applying federal law, the Court holds that if equitable considerations do not produce an unjust result, the general rule as stated in *Crane* will apply.

In determining the remedy for the plaintiff who obtains a decision that a state law is unconstitutional, state law applies. As the Supreme Court stated in *Texas Monthly, Inc. v. Bullock*, 489 U.S. 1, 8, 109 S.Ct. 890, 896 (1989),

> It is not for us to decide whether the correct response as a matter of state law to a finding that a state tax exemption is unconstitutional is to eliminate the exemption, to curtail it, to broaden it, or to invalidate the tax altogether.

The mission, then, of this Court is clear. It must determine, applying federal law, the effect of *Davis* on Arizona

individual income tax law. Unless the effect is non-retroactivity, the Court must then determine a remedy applying state law.

In *Davis,* the state conceded that a refund would be appropriate if the court determined that the Michigan tax scheme was unconstitutional. *Davis,* 489 U.S. at 817. Therefore, *Davis* did not decide non-retroactivity either way. It did, however, express a qualification if the decision were to have retroactive effect. *Davis* held that "the Constitution does not require" a state to invalidate its entire income tax law. *Davis,* 489 U.S. at 817.

In this case, the general rule cannot be applied absolutely to reach the result urged by the Taxpayers. The statute which imposes a tax on the Taxpayers' federal pensions is A.R.S. § 43-1011. If the general rule is applied and A.R.S. § 43-1011 is declared void, the result the Taxpayers want has been achieved. It has also voided all pre-*Davis* individual income taxation in Arizona. *Davis* said specifically that "such a drastic solution" was not necessary. *Davis,* 489 U.S. at 817.

If the Court holds that *Davis* invalidates something less than the statute which imposed the offending tax, then the Court must determine what its holding is going to invalidate and just what the impact of such an invalidation is to be. In doing so, the Court must determine whether its holding will produce an unjust result. In short, the effect of invalidating law must be determined by applying principles of equity.

In this case, the Court applies the general rule, holding that the invalidation of A.R.S. § 43-1011 is, by the very words of *Davis,* too drastic a course for the Court to take. However, the Court can remove the unconditional impediment proscribed by *Davis* by holding invalid former A.R.S. § 43-1022(3) and A.R.S. § 43-1022(4). This the Court has effectively done in its ruling on April 6, 1990. *Bohn v. Waddell,* 164 Ariz. 74, 790 P.2d 772

(Tax 1990). When a law is determined to be void because it is in violation of the constitution, and the constitutional impediment can be removed by the invalidation of alternative statutory provisions, those provisions will be invalidated which do the least violence to the statutory scheme. *State v. Prentiss*, 163 Ariz. 81, 786 P.2d 932 (1989) (entire statute should not be declared unconstitutional if unconstitutional portions are severable); *accord Cohen v. State*, 121 Ariz. 6, 588 P.2d 299 (1978); *State v. Dykes*, 163 Ariz. 581, 789 P.2d 1082 (App. 1990); *United States v. Molina*, 688 F.Supp. 819, 825 (D.Conn. 1988) (court should strive to sever only those provisions of the law that are objectionable).

Such a step makes taxable in retrospect Arizona pensions and the first $2,500.00 of civil service pensions. This satisfies the prospective *Davis* mandate of equal treatment. *Davis*, 489 U.S. at 817-18.

Since the Court has applied the general rule, the remedy is to be determined by state law, subject to the constitutional parameters imposed by the federal constitution and federal law interpreting it. The effect of *Davis*, as decided herein, is that the subtractions from Arizona income authorized in former A.R.S. § 43-1022(3) and A.R.S. § 43-1022(4) are void. Therefore, the State of Arizona has failed to collect taxes from Arizona pensioners and from civil pensioners, for which such pensioners were liable. It could be argued that such a failure constitutes a discriminatory enforcement of the income tax laws.

Income taxes are inherently discriminatory. A graduated income tax discriminates against those in the higher brackets, and in favor of those in the lower ones. The failure to collect taxes from Arizona pensioners and civil service pensioners discriminated against not only non-civil service federal pensioners, but against every taxpayer in whatever category who was required to pay an Arizona tax on income. This discrimination occurred because a

legislated tax benefit has been determined to be unlawful. Where a tax benefit made available to a minority of taxpayers is invalidated, the equal protection clause of the Fourteenth Amendment does not require a retroactive invalidation of the entire tax scheme because of the discrimination created by the invalidation of the benefit. The applicable federal law in this circumstance is clearly that set forth in *Davis*. *Davis*, as has been stated, does not require such a drastic result.

To hold that the Taxpayers are entitled to the full refund they demand would be to create a retroactive tax benefit. The Court is of the opinion that such a step would be beyond the power of this Court or, indeed, any court. The bestowal of income tax benefits is solely the province of the legislature. The evidence presented to the Court demonstrates that such a remedy would have a devastating effect on state finances, the cost of which would have to be borne by all taxpayers, not just those who have enjoyed Arizona pension income. It is clear to the Court that, because of the grevious fiscal disruption such a tax benefit would cause, it is inconceivable that, had the legislature known that the disparate treatment of government pension income was unconstitutional, it would ever have extended the benefit to federal pensioners. It would simply have enacted no benefit at all, or a partial one, as it did, post-*Davis*. A.R.S. § 43-1020 (West 1990).

Because of the adverse financial consequences on other taxpayers not connected with this case, of a remedy such as the Taxpayers claim, and because of the unwarranted benefit to the Taxpayers from such an order, the Court finds that the decision the Taxpayers want would be most unjust. If this were to be the effect of *Davis* required by federal law, then the third prong of *Huson* would be met, and *Davis* would apply non-retroactively. The remedy sought by the Taxpayers is not required by either state or federal law.

The Taxpayers, however, did suffer an injury because of the discriminatory tax. They paid more tax than they would have had to pay had the voided subtractions not been in place. Therefore, they are entitled to be refunded the difference between what they paid and what they would have paid. The formula set forth in the Court's Opinion of April 6, 1990, attempts to define such a refund.

In *McKesson,* Florida argued that, had Florida been aware that its tax was unconstitutional, it would not have enacted the discriminatory favorable rates. Therefore, all taxpayers would have been taxed at the higher rate and so the favored taxpayers would have paid the same thing as the *McKesson* taxpayers. Therefore, the *McKesson* taxpayers were not injured and should not have any tax refunded.

The Taxpayers point out that the *McKesson* court rejected this argument. There are at least three distinguishing factors between this case and *McKesson.* The Supreme Court felt that *McKesson's* injury flowed, not from the fact that it had to pay more tax than the favored taxpayers, but from the fact that as a result it experienced and suffered an economic disadvantage because the favored taxpayers were commerical competitors. That circumstance does not exist here.

Although Florida claimed that the invalidation of its tax was not reasonably pre-foretold by earlier decisions of the court, it is clear from a reading of the *McKesson* Opinion that Justice Brennan, at least, considered the Florida scheme a thinly veiled attempt to retain in place a tax scheme that had been invalidated in *Bacchus Imports, Ltd. v. Dias,* 468 U.S. 263, 104 S.Ct. 3049, 82 L.Ed.2d 200 (1984). *McKesson,* 110 S.Ct. at 2255. It was the opinion of the *McKesson* Court that Florida should have known that its scheme was a constitutional violation. *Smith,* 110 S.Ct. at 2333.

In this case, the Court has held that *Davis* announced a new principle of law. *Bohn v. Waddell*, 164 Ariz. 74, 86, 790 P.2d 772, 783 (Tax 1990). Finally, the rejected Florida solution resulted in no remedy at all.

McKesson specifically approved the approach this Court has taken. *McKesson*, 110 S.Ct. at 2251-52. In *Smith*, Justice Stevens said:

> Our opinion today in *McKesson Corp. v. Division of Alcoholic Beverages*, makes clear that the Federal Constitution does not require the State to refund the entire tax that was unconstitutionally exacted from petitioners, but only to refund the discriminatory portion or otherwise adjust the tax to render it non-discriminatory.

Smith, 110 S.Ct. at 2346 n.2 (Stevens, J., dissenting).

The remedy is also authorized under *Bade v. Drachman*, 4 Ariz. App. 55, 63-64, 417 P.2d 689, 697 (1966); and *Pittsburgh and Midway Coal Mining Co. v. Department of Revenue*, 161 Ariz. 135, 776 P.2d 1061 (1989). The Court, therefore, reaffirms, in light of the four U.S. Supreme Court cases reviewed, the decisions made and annouced in its earlier Opinion in this case, *Bohn v. Waddell*, 164 Ariz. 74, 790 P.2d 772 (Tax 1990).

/s/ William T. Moroney
WILLIAM T. MORONEY
Judge of the Arizona Tax Court

This Opinion Filed: March 7, 1991

APPENDIX E

IN THE SUPERIOR COURT
OF THE STATE OF ARIZONA
IN THE ARIZONA TAX COURT

No. TX 89-00050

JOHN L. and SHIRLEY BOHN, husband and wife,
DONALD and MARY RUTAN, husband and wife,
and CARL LINTON, a single man, *et al.*,
Plaintiffs,

vs.

PAUL WADDELL, individually and as Director of the
Department of Revenue of the
State of Arizona; *et al.*,
Defendants.

ORDER

The Court, having considered Intervenors' Motion to Intervene and having denied same,

IT IS HEREBY ORDERED denying the Motion to Intervene.

DONE IN OPEN COURT this 20 day of June, 1990.

/s/ William T. Moroney
Judge
Superior Court of
Maricopa County

APPENDIX F

IN THE SUPERIOR COURT
OF THE STATE OF ARIZONA
IN THE ARIZONA TAX COURT

No. TX 89-00050

(Assigned to the Honorable William T. Moroney
Division 11)

ESTATE OF JOHN L. BOHN, SHIRLEY BOHN,
DONALD AND MARY RUTAN, husband and wife,
and CARL LINTON, a single man,
Plaintiffs,

vs.

PAUL WADDELL, individually and as Director of the Department of Revenue of the State of Arizona; J. ELLIOT HIBBS, individually and as former Director of the Department of Revenue of the State of Arizona; BETSEY BAYLESS, individually and as former Director of the Department of Revenue of the State of Arizona; RUSSELL RITCHIE, individually and as former Director of the Department of Revenue of the State of Arizona; MIKE WOLFE, individually and as former Director of the Department of Revenue of the State of Arizona; REX WAITE, individually and as former Director of the Department of Revenue of the State of Arizona; C. HOS HOSKINS, individually and as former Director of the Department of Revenue of the State of Arizona; JOHN DOE I-V and JANE DOE I-V, individually and as former Directors of the Department of Revenue of the State of Arizona; JOHN ROE I-X AND JANE ROE I-X are the spouses of the individual Defendants who were or are the Directors of the Department of Revenue of the State of Arizona; and all the unknown agents, em-

ployees, successors in office, assistants and all others acting in concert or cooperation with the current and former Directors of the Department of Revenue of the State of Arizona, or at the direction of the current and former Directors of the Department of Revenue of the State of Arizona, and the DEPARTMENT OF REVENUE OF THE STATE OF ARIZONA,

Defendants.

JUDGMENT

This matter having come on for decision and the Court having considered the Second Amended Complaint, the answer thereto, the motions of the parties, the extensive filings in support thereof, the briefs and arguments of counsel, and all of the records and proceedings heretofore had in this action, the Court renders judgment in full accord with and as more particularly set forth in *Bohn, et al. v. Waddell, et al.*, 164 Ariz. 74, 790 P.2d 722 (Ariz. Tax 1990), including Appendix A, of this April 6, 1990, published Opinion. The foregoing Opinion is attached hereto as Exhibit 1 and is incorporated in this Judgment by this reference.

A. With respect to the First Claim for Relief of Plaintiffs' Second Amended Complaint, it is found, ordered, adjudged and decreed as follows:

(1) Plaintiffs are not required to exhaust administrative remedies prior to bringing a claim under 42 U.S.C. § 1983 in the Arizona Tax Court.

(2) The Court grants summary judgment to all Defendants on the First Claim for Relief, holding that the Plaintiffs have no claim based on 42 U.S.C. § 1983 against the State or against the individual Defendants in their official capacities. Neither the State nor its officials acting in their official capacities are persons under § 1983. Further, the Court holds that the right which

the Plaintiffs claim that the individual Defendants violated was not clearly established before *Davis v. Michigan Dep't of Treasury*, —— U.S. ——, 109 S.Ct. 1500, 103 L.Ed.2d 891 (1989), was decided by the U.S. Supreme Court. The individual Defendants in their individual capacities are entitled to qualified immunity from suit brought under 42 U.S.C. § 1983.

B. With respect to the Second Claim for Relief of Plaintiffs' Second Amended Complaint, it is found, ordered, adjudged and decreed as follows:

(1) Plaintiffs are not required to exhaust administrative remedies before bringing suit in the Arizona Tax Court under the circumstances of this action. The issue which gives rise to Plaintiffs' claim is whether a taxing statute is constitutional, an issue which cannot be resolved on the administrative level. An administrative body has no power to determine whether a statute complies with a constitution. Furthermore, the administrative process would not provide an adequate remedy.

(2) The Court determines that one or more of the named Plaintiffs paid Arizona income taxes on federal pension income in each of the tax years 1984 to 1988.

(3) The Court grants summary judgment to the Plaintiffs on the Second Claim for Relief. Prior to a 1989 amendment and during the tax years 1984 to 1988, A.R.S. § 43-1022(3) allowed a subtraction from Arizona gross income for pensions paid by Arizona State and local governments to retired Arizona State and local governmental employees. A.R.S. § 42-1022(4) allowed a subtraction of $2,500 from Arizona gross income for federal civil service retirement income. There was no subtraction provided for pension benefits from any federal retirement program other than civil service. The Court declares that this tax scheme was in violation of 4 U.S.C. § 111 and the doctrine of intergovernmental tax immunity; further, the scheme discriminated against

both civilian and military retirees and in favor of State retirees. It also discriminated in favor of federal civil service retirees and against other federal retirees. The Court finds no distinction for purposes of this case between military retirees and any other federal retirees. The justification for giving favorable tax treatment to state pensioners offered by the Department here is sustainable under equal protection standards.

(4) Plaintiffs are entitled to a refund remedy for Arizona income taxes paid by them with respect to federal retirement benefits for the tax years 1984 through 1988. The Court finds that the first prong of *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971) is satisfied. The Court, however, does not find that there is any serious inequity in a refund to Plaintiffs that reimburses them for the economic loss incurred as a result of the constitutional violation. The measure of the extent that the exemptions set forth in A.R.S. § 43-1022(3) and (4) discriminated against federal retirees is the amount of the tax paid by federal retirees that is greater than they would have paid if A.R.S. § 43-1022(3) and (4) had not been in place.

(5) The amount of the refund to which Plaintiffs and, pursuant to this Court's order of virtual representation, all similarly-situated retired federal employees are entitled shall be calculated independently for each of the years 1984 to 1988 in two steps. In step one, the Department of Revenue shall multiply .0275 times the individual taxpayer's marginal (highest) Arizona income tax rate and multiply the product thereof times the federal pension income of the individual taxpayer. In step two, if income has been subtracted pursuant to A.R.S. § 43-1022(4), the amount of such income subtracted must be multiplied by the taxpayer's marginal (highest) Arizona tax rate and subtracted from the amount determined in step one. If no income was subtracted pursuant to A.R.S. § 43-1022(4), the amount determined under step one is the refund. If step one minus step two is

less than or equal to zero, the refund is zero. No more tax can be refunded than was paid.

(6) The Department shall calculate and pay interest on the sums to be refunded at such rates as the Department pays on income tax refunds.

C. It is further ordered, adjudged and decreed as follows:

(1) The Court declares, pursuant to A.R.S. § 12-1831, *et seq.*, that the Arizona income tax scheme for taxing federal and state pensions, as it existed before the 1989 amendment to A.R.S. §§ 43-1022(3) and (4), was in violation of 4 U.S.C. § 111 and the federal constitutional doctrine of intergovernmental tax immunity. The right violated is not an individual fundamental right guaranteed to the Plaintiffs, but is a right inuring to the United States.

(2) As to both claims for relief, the Court denies Plaintiffs' Motion to enjoin enforcement of the Arizona law which imposes an income tax on federal pensions and to enjoin further collection of Arizona income taxes due but not paid by federal retirees for tax years prior to 1989 for that part of the retired federal employee's Arizona income tax liability which is attributable to the inclusion of federal pension income in Arizona taxable income.

(3) Since the Arizona Legislature has repealed the offending tax scheme complained of, enforcement for tax years beyond 1988 is no longer a duty imposed on the Department. With regard to further collection, the Court finds that the Plaintiffs and all persons virtually represented will suffer no irreparable harm if the injunction is not issued. The Court declines to order injunctive relief.

(4) The Court denies Plaintiffs' Motion for Class Certification with respect to both the First and Second

Claims for Relief. The Court orders virtual representation in accordance with its published Opinion of April 6, 1990 and directs the Department of Revenue to treat all persons who paid Arizona income tax on federal pensions for tax years 1984 through 1988 as though each such person were a named Plaintiff on the Complaint herein. Applications for refunds may be made up until the first April 15th two years after there is a final unappealable decision in this matter or until the expiration of the term provided in A.R.S. § 42-115, whichever is later. Notice to affected persons shall be in accordance with the Court's published Opinion of April 6, 1990.

(5) Defendants' Counterclaim based on A.R.S. § 42-133 is dismissed without prejudice by stipulation of the parties. In addition, defendant Rex Waite is dismissed as a defendant in this action by stipulation of the parties, such dismissal to be with prejudice.

(6) Plaintiffs are entitled to recover from the Defendant Arizona Department of Revenue attorneys' fees in the amount of $105,000.00 under A.R.S. § 12-348 and costs in the amount of $2,128.56.

DONE IN THIS OPEN COURT this 7 day of March, 1991.

/s/ William T. Moroney
WILLIAM T. MORONEY
Judge
Arizona Tax Court

APPENDIX G

SUPREME COURT

STATE OF ARIZONA
402 Arizona State Courts Building
1501 West Washington
Phoenix, Arizona 85007-3329

Telephone: (602) 542-9396

NOEL K. DESSAINT
Clerk of Court

KATHLEEN E. KEMPLEY
Chief Deputy Clerk

April 14, 1993

RE: ESTATE OF JOHN L. BOHN/SHIRLEY BOHN/DONALD RUTAN *et al* vs. PAUL WADDELL/DEPT OF REVENUE/CRAIG CORMIER *et al*
Supreme Court No. CV-92-0452-PR
Court of Appeals No. 1 CA-TX 91-008
Tax Court No. TX 89-00050

GREETINGS:

The following action was taken by the Supreme Court of the State of Arizona on April 13, 1993, in regard to the above-referenced cause:

ORDERED: Petition for Review by the Arizona Supreme Court = DENIED.

Record returned to Court of Appeals, Division One, Phoenix this 14th day of April, 1993.

NOEL K. DESSAINT
Clerk

APPENDIX H

SUPREME COURT

STATE OF ARIZONA
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1501 West Washington
Phoenix, Arizona 85007-3329

Telephone: (602) 542-9396

NOEL K. DESSAINT
Clerk of Court

KATHLEEN E. KEMPLEY
Chief Deputy Clerk

April 14, 1993

RE: PAUL WADDELL *et al* vs. ARTHUR J. ABBOTT/MARY J. ABBOTT/FRED ABENDSCHEIN, *et al*
Supreme Court No. CV-92-0445-PR
Court of Appeals No. 1 CA-TX 90-0029
Tax Court No. TX 89-00050

GREETINGS:

The following action was taken by the Supreme Court of the State of Arizona on April 13, 1993, in regard to the above-referenced cause:

ORDERED: Petition for Review by the Arizona Supreme Court = DENIED.

Record returned to Court of Appeals, Division One, Phoenix this 14th day of April, 1993.

NOEL K. DESSAINT
Clerk

APPENDIX I

LIST OF PARTIES PURSUANT TO RULE 14.1(b)

Arthur J. Abbott
Mary L. Abbott
Fred Abendschein
William A. Abolt
Theodore W. Abraham
John D. Abrahamson
Mary A. Abril
Ruben E. Acosta
Doris I. Adams
Dorothy J. Adams
Harold I. Adams
Harold C. Adams
John Q. Adams
Martha P. Adams
Robert L. Adams
Shigeko Adams
Stewart H. Adams
Thom H. Adams
Harold Q. Adams, Jr.
William A. Adams, Jr.
Wayne L. Adamson
Myron F. Addison
Oscar J. Adler, Jr.
Robert W. Adrian
Joe P. Aguirre, Jr.
George S. Ahrens
Charles E. Ahring
Charles W. Ainsworth
Edward J. Aitken
Miriam H. Aiton
Joshua B. Akers
Lillie B. Akers
Paul C. Akin
William P. Akins
Betty Albert
Margaret C. Albin
Robert B. Albrecht
Ralph N. Albright
George E. Albright, Jr.
George F. Alces, Jr.
Merle H. Alden
Victor W. Alden
Marilyn Alderete
Zora Aldrete
Aileen Allen
Benjamin R. Allen
George H. Allen
Helen M. Allen
James J. Allen
Margerie N. Allen
Richard L. Allen
William J. Allen
William H. Allen
Nathan A. Allen, Jr.
William C. Allen, Jr.
Robert V. Allen, Sr.
James R. Allinger
Kenneth W. Allison
Joseph R. Allman
Walter S. Alpert
William E. Alsabrook
George Alstad
Joe R. Alvarez
Jose H. Amador
Kathaleen E. Ames
Katherine Amess
Eunice O. Amundson
Lowell O. Amundson
David O. Andersen
Arnold V. Anderson
Charles D. Anderson

Charles G. Anderson
Donald N. Anderson
Eugene B. Anderson
Eugene B. Anderson
John E. Anderson
John W. Anderson
John E. Anderson
John T. Anderson
Kenneth R. Anderson
LeRoy A. Anderson
Mary W. Anderson
Muriel M. Anderson
Orval N. Anderson
Ralph L. Anderson
Robert W. Anderson
Russell E. Anderson
Warren C. Anderson
William D. Anderson
Andrew A. Andress
Kaml Andrew
Aldine H. Andrews
Alice G. Andrews
Vernon F. Andrews
Mildred J. Andrick
John J. Angel
Michael D. Angiulo
Charles C. Annand
Wilma A. Anspach
Joel A. Anthony
Leon N. Anthony
Joseph W. Antoides
Lui J. Antonelli
James P. Antonopulos
Harvey B. Apperson
Lewis A. Apple
Mary A. Applegate
Harvey G. Appleton
Helen E. Appleton
David M. Archer
Ray M. Archer
Richard F. Archer, Jr.
Julio J. Arias
Charles E. Armijo
Ulysses W. Armijo
Delight R. Armstrong
Ivan O. Armstrong
Clyde E. Arnett
David W. Arnett
Ray R. Arnett
Howard E. Arney
Budd A. Arnold
Evelyn E. Arnold
George C. Arnold
Joseph F. Arnold
Will J. Arnold
William S. Arnott
Joseph Aronson
Leo J. Arsenault
W. P. Arthur
Robert Arzaga
Ivan Asay
Dolores M. Ash
Albert O. Ashby
Robert C. Ashdown
W. F. Ashenfelder
Jerry W. Asher
Robert L. Asher
Fred M. Ashley
James R. Ashworth II
Jonathan M. Askew
Pauline Askin
Harry Atkinson, Jr.
Nadine A. Attebery
A. G. Atwater
Charles L. Atwood
Floyd V. Auckly
Estate—
George E. Aufderheide

James A. Augstine
Burt M. Aukerman
Allie M. Austin
Carol F. Austin
Sidney A. Austin
Fernallen A. Auxier
John Avriette
Gordon Axberg
B. Isalea Axford
C. W. Axsom
Nathan L. Axton
Stephen C. Ayres
Marcus D. Baca
John A. Bach
Thomas Bacome
Charles C. Bacon
Stanley E. Bacon
Forrest C. Bacus, Jr.
Dean M. Baer
Raymond W. Baethke
Ray D. Bafus
Chester H. Bahn, Jr.
William J. Baierschmitt
Kenneth C. Bailey
May H. Bailey
Norman G. Bailey
R. L. Bailey
Travis Bailey
Gerald L. Baird
Dilworth Baird, Jr.
Palmer M. Baken, Jr.
Clarence A. Baker
Floyd E. Baker
Harrison L. Baker
Mable M. Baker
Neil B. Baker
Perry S. Baker
Walter T. Baker
Lyle A. Baker, M.D.

James J. Balamenti
Majorie A. Balbo
Liese R. Baldanza
Arnold Balderrama
Constance Baldwin
Edward J. Ball
Laura E. Ball
Sheila S. Ball
Delbert L. Ballard
Sam H. Ballard
George R. Ballowe
Julie M. Ballweg
Eugene F. Balstad
Charlotte M. Baltz
John Baner
William L. Bangs
Frank Banicevich
Ruth W. Bannister
E. L. Baptist
Gerald A. Baranowski
James R. Barber
Mary M. Barham
Buford P. Barickman
A. E. Barker
Meredith D. Barnard
Thomas H. Barnard
Jack A. Barnes
Joseph P. Barnes
Ruby E. Barnes
William E. Barnes
Peter L. Barone
Allen H. Barr
Roberto Barrera
Robert L. Barrett
John P. Barron
Daniel E. Barrow
Frank J. Barry
Lawrence W. Bartee
George E. Bartell

Richard L. Barter
Claude A. Barth
Robert C. Barth
Elwin F. Bartholomew
George E. Bartlett
J. C. Barton
George T. Bass
Ruth E. Bass
Winfred E. Bass
Duane D. Bassen
Ida L. Bassett
Richard M. Batchelder
Charles C. Bates
Enid Y. Bates
Thomas F. Bates
Francis W. Battaglia
Joseph A. Battaglia
Helen E. Batten
Wilbert L. Battle
Raymond R. Battreall
Rex D. Baucom
Arthur E. Bauer
John Bauer
Paul E. Bauer
June E. Bauers
Betty S. Baughman
Marian S. Bauhs
Aaron H. Bauman
George F. Bauman
Wilbur W. Baur
Ralph A. Baxa
Robert L. Baxter
Andrew V. Baylor
Donald W. Bayne
Lewis N. Bayne
Dorohty W. Beamis
Joseph M. Bean
William Bean
Lawrence Bearson
Lesley B. Beatty
Margaret D. Beaver
Clair F. Beck
Stanley C. Beck
James E. Becker
Olah D. Becker
Charles Beckman
Charles J. Beckman
John A. Beckman
Wilma Becknell
Ralph L. Beckwith
John M. Beeler, Sr.
Sheldon T. Beeman
Ray D. Beesley
Lorene H. Beets
Julius A. Begonia
Harold N. Behm
Michael Behun
Vernon C. Beier
Theodore Beim
Lorraine W. Beland
Dale M. Belcher
Elizabeth F. Belcher
Hugh Belden
Alfred L. Bell
Faye V. Bell
Robert G. Bellemare
June M. Bellingham
Samuel Benjamin
Beatrice F. Bennett
Charles W. Bennett
Hassie R. Bennett
Carolyn W. Benson
Edwin Benson
Estate—Charles A. Benson
June C. Benson
Lois W. Benson
Mollie S. Benson
Elinore M. Bentley

Frank E. Bentley
James A. Bentley, Jr.
Gordon F. Berg
Janet Berg
Gustaf E. Berglund
Gilbert A. Bergman
Reuben P. Bergman
Elizabeth B. Bergstedt
George Berletic
Eugene Berlin
Virginia D. Berlin
Charles E. Bernard
Irene P. Bernardoni
Margaret P. Brendt
Wilfred L. Brendt
Kenneth V. Bernstrom
Donald L. Berry
Helen E. Berry
James M. Berry
Elizabeth T. Bershenyi
Richard P. Bertagni
C. A. Besser, Jr.
Philip H. Best
Olivia E. Beste
J. W. Bethard
Frank W. Betz
Margaret Beveridge
Netta R. Bey
Vernon L. Biaett
Blanche B. Bickel
John C. Bickers
J. E. Bicknell
Irvin A. Bielas
Charles P. Bigelow
Roy F. Bigelow
William W. Bigler
Helen E. Bildenback
Dwight L. Bilharz
J. H. Bilkey
Maro T. Bingham
Silas B. Birch, Jr.
Silas B. Birch, Jr.
Robert C. Birkett
Frank E. Birtciel
Gordon A. Bishop
Gordon F. Bishop
Richard J. Bishop
Rolla M. Bishop, Sr.
William Bittens
Harry E. Bittner
Arthur L. Bivens
Orville H. Bjorge
Earl M. Black
Joe B. Black
Raymond A. Black
Robert E. Black
Kay S. Blackman
Van O. Blackman
Jack R. Blackway
Garrett E. Blackwell
Eldon E. Blair
Ferne M. Blair
James E. Blakeslee
Mary E. Blakeslee
William B. Blanchet
Richard J. Blanco
G. F. Blankinship
C. F. Blanton
Mary E. Blassingame
Gladys M. Blegen
Edwin E. Blessing
George A. Blier
Marian T. Block
Eileen C. Block
Dorothy A. Blocksom
Benjamin V. Blom
Robert N. Blomstrand
Douglass K. Blood
Janet B. Bloom

Margaret Blovits
Virgil E. Bloyd
Adolf Blum
Margaret E. Blumenthal
Lester C. Board
Ollie L. Boat
Dale M. Boatman
Emily J. Boatwright
Frank J. Bobek
Joyce J. Bodenhammer
Theodore F. Bodnar
Frederick E. Boesch, Jr.
Francis J. Boger
Ernest Boghosian
John L. Bohn
John W. Bohning
Francois A. Boivin
Vincent J. Bokoski
Donald H. Bolander
James P. Boles
John A. Bollan
Charles R. Bollenberg
Horace G. Bolser
Abraham F. Boltares
William C. Bolton
Robert J. Boltz
Della M. Bomar
Ronald Bond
Orvel L. Bonds
Elizabeth J. Bonnell
Robert E. Bookman
Charlie Boom
William B. Boomhower
Elizabeth M. Boone
Richard M. Boone
Boyd L. Booth
Lillian M. Borcherding
Eugene J. Bordas, Jr.
Joyce A. Bordner
Roy C. Borg
Robert L. Borgos
Alice M. Boring
Junior D. Borrow
Junior D. Borrow
Casimir Borysiewicz
Gwen Bosley
John R. Boston
Margaret J. Boswell
Eugene M. Botts
Robert H. Botts
Ralph A. Bouckhuyt
Pearl C. Bough
Raphael D. Bourrie
Robert J. Bower
Roscoe O. Bowers
Joseph E. Bowie
Charles A. Bowman
Elmo L. Bowman
Edward H. Boyd
Irma I. Boyd
Robert L. Boyd
Paul G. Boyer
Richard H. Boyer
Sam L. Boyette
Agnes J. Boyle
Edward L. Boyle
James P. Boyle
Edward E. Boyles
Martha F. Bradeen
Raymond T. Bradley
Blaine Bradshaw
Orrin L. Bradshaw
Charles J. Brady
Francis R. Brady
William C. Brady
Angela D. Bragg
Frank S. Braje
Ralph Braley

Wallace H. Brammann
George Brandstetter
Jerome N. Brandt
Cleone A. Branham
William T. Branham
Katherine M. Brannan
Gerald P. Brannon, Jr.
John O. Braun
Margaret C. Braun
Benjamin M. Bravence
Horace A. Brawley
James O. Brazell
Janet W. Brecheen
Wilburn C. Brecheen
Violet G. Breckenridge
Garold G. Breeding
James M. Breen
Eugene W. Brees
Theodore A. Brees
Clarence D. Brehm
Elizabeth L. Breitung
Lillian L. Breitzke
Garland E. Brenneman
Herbert H. Breves
C. W. Brewster
Martin L. Brewton
Rayburn L. Brians
Aloysius J. Brick
Brent N. Bridges
James S. Briggs
Edward J. Brink
Russell C. Brinker
Elsie M. Brinley
Dorise R. Brisbin
Robert A. Bristow
Dorothy H. Britt
J. M. Broadbent
George B. Brockway
Irwin H. Brodsky
John D. Brooks
Charles H. Brown
Cleo B. Brown
Dorothy M. Brown
Dorothy E. Brown
Edith M. Brown
Edith M. Brown
Fred J. Brown
Howard O. Brown
Howard L. Brown
Jacobs V. Brown
James R. Brown
James R. Brown
John M. Brown
Kent A. Brown
Liesel Brown
Lloyd H. Brown
Luevenia B. Brown
Margaret L. Brown
Mary Louise Brown
Milo G. Brown
Ocee G. Brown
Ray E. Brown
Richard N. Brown
Robert C. Brown
Rodney G. Brown
Walter J. Brown
Walter G. Brown
Walter Z. Brown
William M. Brown
Winton C. Brown
Richard H. Bruce
Leonard E. Bruens
James R. Brugman
Robert L. Brummet
John H. Bryan
George A. Bryant
Dorman J. Bryce
Wallace E. Bryce

Carolyn A. Buchanan
Doris F. Buche
Walter P. Buck
Joe T. Buckler
Bernard T. Buckley
Clark H. Buckley
George M. Buckley
Francis F. Buckmaster
Robert B. Buckmaster
Joseph C. Bueche
Robert O. Buffington
Joseph C. Bugeya
Eugene E. Bullock
Marvin C. Bullock
Robert B. Bunker
Harry E. Bunting
Lawrence T. Burback
Jeanne B. Burbank
Mildred O. Burbank
Earl Burden
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Harold W. Burdine
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Ronald A. Burgher
David F. Burgoon
Claude E. Burk
Albert H. Burkhardt
Lee L. Burklund
Walter W. Burleigh
Frank W. Burnett
Mildred A. Burns
Pauline Burns
Herman R. Buros
Marjorie E. Burris
Donald Burroughs
Frances L. Burrow
Stanley Burstiner
John E. Burt
George C. Burton
James E. Burton
Stanley G. Burton
Audrey L. Busby
Floyd T. Buser
James L. Bush
Richard B. Bushong
Joseph M. Buswell
Eizabeth L. Butler
Harold A. Butler
Harold W. Butler
Marjorie J. Butler
Rosita K. Butler
William C. Butler
Blaine R. Butler, Jr.
Joseph C. Butner
Arthur A. Buxton
John H. Buzard
Victor N. Byerly
Alice E. Byers
Daniel R. Bynum
Thomas F. Byron
Woodrow W. Caber
Marcel R. Cadrin
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Naomi F. Cain
Gerald Caldwell
Anne E. Caldwell, M.D.
Angelo Caliern
Leslie F. Calkins
Frederick W. Call
George F. Callaghan
Robert M. Callaghan
John L. Callahan
Virginia P. Callahan
Rual G. Callan

Grove K. Callison
Joseph V. Camasto
James E. Cambern
Charles E. Cameron
Robert R. Campaigne
Barbara F. Campbell
Bernice J. Campbell
Florence J. Campbell
Marjorie L. Campbell
Patrick A. Campbell
R. Edward Campbell
Ruby L. Campbell
Ruth L. Campbell
William A. Campbell
William K. Campbell
William H. Campbell
Richard P. Campbell, Jr.
Elizabeth J. Camphuysen
George W. Candish
Andrew O. Cannaliato
Edward W. Cannon
Fred J. Cannon
Marshall R. Canter
James A. Cantrell
Frances J. Capone
John P. Capp
Lawrence W. Capps
Winifred L. Caraway
Edith D. Carbonelli
John H. Cardellina
Christopher J. Carey
Nelson B. Carey
Paul J. Carlberg
William J. Carlberg
E. William Carlbom
Ruth L. Carlin
Conrad E. Carlson
Duane D. Carlson
Ernest T. Carlson
Glenn H. Carlson
William S. Carlton
Don B. Carmichael
Don Carmichael
John C. Carmody, Jr.
Andrew B. Carnahan
Charlie L. Carnahan
Burel D. Carney
Earl E. Carney
Eldra M. Carney
Harold E. Carney
Kenneth L. Carpenter
Kirk Carpenter
Neil K. Carr
Roderick A. Carr
Lewis G. Carrifee
Clifford C. Carrigan
Joseph F. Carroll
Wilson C. Carroll
Jane H. Carson
Robert F. Carson
Harlon B. Carter
Harold W. Carter
Louise Carter
Warren E. Carter
Bernadette Cary
Donald R. Cary
Ben J. Case
Oscar W. Case
Raymond H. Case
Dudley F. Casler
Rita C. Cassidy
Norma A. Cassoday
Jesus L. Castaneda
Gladys G. Caster
Mary J. Catey
Dale K. Causey
William E. Causey
Ferdinand E. Cauwels

Amelia B. Cazier
Ysidoro A. Ceballos
Raymond G. Cech
D. John Cederstrom
Laura F. Celaya
Victor E. Celio
Nicholas C. Cellino
Merlin J. Chadsey
Joseph G. Ghaet
Dorothy Chairella
Fred S. Chamberlain
Roland J. Chamberlain
William E. Chamberlain
Roland J. Chamberlain, Jr.
Donald W. Chambers
Verlin N. Chandler
Benjamin P. Chaney
Peter A. Chaplik
Evelyn L. Chapman
Lois W. Chapman
Williard E. Chapman
Lawson E. Chappell
Charles M. Chartier
Taris Charysyn
Hazel I. Case
Leland D. Chase
Charles H. Chassot
Edward Cheney
Malvin J. Chernow
Jack A. Chewning
James E. Chikar
Paul E. Childress
Marie E. Childs
Norma Chiles
Cecil W. Chisholm
Ruth G. Chosiad
Edward Chrisman
Isabelle T. Christen
Charles M. Christenberry
Arthur B. Christensen
Laverne E. Christensen
Joseph F. Christopher
George Church
Helen L. Church
Anthony E. Ciampa
Angeline L. Cimino
Lee H. Cinnamon
James W. Clabaugh
Perry V. Clarence
Elizabeth (PR) W. Clark
Fairie B. Clark
Gloria O. Clark
Harry E. Clark
Herman H. Clark
James H. Clark
James P. Clark
John H. Clark
Kenneth B. Clark
Maxine Clark
Randall L .Clark
Richard S. Clark
Vernon M. Clark
Wenona C. Clark
Will M. Clark
Kermit Clark, Sr.
Charles E. Clarke
Robert P. Clarke
Harry J. Clary
Norman W. Claytor
Raymond C. Cleghorn
Stanley Cleghorn
Lyle B. Clemans
Charles P. Clemens
Virginia Clement
William S. Clement
Halbert B. Clemmer
O'Reece O. Cleve

Knowles C. Clifton
Ester E. Cline
Harold F. Cline
James M. Clint
Margaret M. Clippinger
John F. Clorus
Fred L. Close, Jr.
Ruth Mildred Clow
Gaylord M. Cloyd
Elsie Coates
Desmond A. Coath
Frank C. Cochran
Gloria E. Cochran
Raymond O. Cochran
Olivine B. Cochrane
John F. Coffin
Lola C. Coffin
Robert Coffin
Seretha Coffin
Stella E. Coffman
Wayne E. Coffman
George W. Coffos
Vera J. Coglizer
Geraldine F. Cohen
Trellis M. Coil
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F. Eugene Smith
Flossie H. Smith
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George D. Smith
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Haddon H. Smith
Jackson R. Smith
James F. Smith
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Joe E. Smith
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Josephine E. Smith
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Marvin W. Zumwalt
Lia R. Zweig

APPENDIX J

EXCERPTS OF RELEVANT PORTIONS OF THE ARIZONA CONSTITUTION, STATE STATUTES AND STATE REGULATIONS

I. RELEVANT PROVISIONS OF THE ARIZONA CONSTITUTION:

Article III—Distribution Of Powers

The powers of the government of the State of Arizona shall be divided into three separate departments, the Legislative, the Executive, and the Judicial; and, except as provided in this Constitution, such departments shall be separate and distinct, and no one of such departments shall exercise the powers properly belonging to either of the others.

Article VI, § 1—Judicial power; courts

Section 1. The judicial power shall be vested in an integrated judicial department consisting of a Supreme Court, such intermediate appellate courts as may be provided by law, a superior court, such courts inferior to the superior court as may be provided by law, and justice courts.

Article VI, § 14—Superior court; original jurisdiction

Section 14. The superior court shall have original jurisdiction of:

* * * *

2. Cases of equity and at law which involve . . . the legality of any tax, impost, assessment . . . .

II. RELEVANT PROVISIONS OF THE ARIZONA REVISED STATUTES ANNOTATED:

Ariz. Rev. Stat. Ann. § 12-123 (1992):

Jurisdiction and powers

A. The superior court shall have original concurrent jurisdiction as conferred by the constitution.

. . .

B. The court, and the judges thereof, shall have all powers and may issue all writs necessary to the complete exercise of its jurisdiction.

Ariz. Rev. Stat. Ann. § 12-124 (1992):

Appellate jurisdiction; issuance of writs

A. The superior court shall have appellate jurisdiction in all actions appealed from justices of the peace, inferior courts, boards and officers from which appeals may, by law, be taken.

Ariz. Rev. Stat. Ann. § 12-161 (1992):

Definition of tax court

A. In this chapter, unless the context otherwise requires, "tax court" means the tax department of the superior court in Maricopa county when exercising the original jurisdiction of the superior court over cases of equity and at law which involve the legality of any tax, impost or assessment.

Ariz. Rev. Stat. Ann. § 12-168 (1992):

Proceedings

A. Proceedings before the court are original, independent proceedings and shall be tried de novo.

B. If an action is an appeal from an order or determination of an administrative agency, the action shall be an original proceeding in the nature of a suit to set aside the order or determination.

Ariz. Rev. Stat. Ann. § 12-910 (1992):

Scope of review

A. An action to review a final administrative decision shall be heard and determined with convenient

speed. The hearing shall extend to all questions of law and fact presented by the entire record before the court. No new or additional evidence in support of or in opposition to a finding, order, determination or decision of the administrative agency shall be heard by the court, except in the event of a trial de novo . . . .

B. The trial shall be de novo if trial de novo is demanded in the complaint or answer of a defendant other than the agency . . . . When a trial de novo is available under the provisions of this section, it may be had with a jury upon demand of any party.

Ariz. Rev. Stat. Ann. § 35-196.03 (Supp. 1992):

Refunds for invalid tax laws; appropriation required

Notwithstanding any provision of law to the contrary, no monies may be paid from the state treasury to refund monies collected under a law imposing a tax if the law is declared invalid by a final judgment of a court of competent jurisdiction until the legislature has made a specific appropriation for that purpose after the judgment has become final.

Ariz. Rev. Stat. Ann. § 42-115 (1991):

Time limitations for credit and refund claims

A. The period within which a claim for credit or refund may be filed, or credit or refund allowed or made if no claim is filed, is the period within which the department may make an assessment under § 42-113.

* * * *

C. The failure to begin an action for refund or credit within the time specified in this section is a bar against the recovery of taxes by the taxpayer.

Ariz. Rev. Stat. Ann. § 42-122 (1991):

Appeal to the department; hearing

A. Except in the case of individual income taxes, a person from whom an amount is determined to be due under this article may apply to the department by a petition in writing within forty-five days after the notice of a proposed assessment made pursuant to § 42-118, subsection B or the notice required by § 42-117, subsection B is received, or within such additional time as the department may allow, for a hearing, correction or redetermination of the action taken by the department. In the case of individual income taxes the period is ninety days from the date the notice is mailed . . . . If only a portion of the deficiency assessment is protested, all unprotested amounts of tax, interest and penalties must be paid at the time the protest is filed. The department shall consider the petition and grant a hearing, if requested. To represent the taxpayer at the hearing or to appear on the taxpayer's behalf is deemed not to be the practice of law.

* * * *

C. All orders or decisions made on the filing of a petition for a hearing, correction or redetermination become final thirty days after notice has been received by the petitioner, unless the petitioner appeals the order or decision to the state board.

Ariz. Rev. Stat. Ann. § 42-124 (1991):

Appeal to state board and to court

A. A person aggrieved by a final decision or order of the department under this article may appeal to the state board . . . . The board's decision is final on the expiration of thirty days from the date when notice of its action is received by the taxpayer, unless either the department or the taxpayer brings an action in superior court as provided in subsection B.

B. The department or a taxpayer aggrieved by a decision of the board may bring an action in superior court subject to the following provisions:

1. No injunction, writ of mandamus or other legal or equitable process may issue in an action in any court in this state against an officer of this state to prevent or enjoin the collection of any tax, penalty or interest.

2. . . . Within the time limits set forth in § 42-115, a taxpayer who fails to protest the payment of any tax illegally or erroneously collected may file a claim for refund of the taxes paid. Such refund claim shall then be governed by § 42-130 and this section. The superior court shall hear and determine the appeal as a trial de novo. . . .

Ariz. Rev. Stat. Ann. § 42-130 (1991):

Denial of refund

A. If the department disallows any claim for refund, it shall notify the taxpayer accordingly. The department's action on the claim is final unless the taxpayer appeals to the department in writing within the time and in the manner prescribed by § 42-122. If the department disallows interest on any claim for refund, it shall notify the taxpayer accordingly and thereafter the claim shall be treated as a claim for refund.

B. If the department fails to mail notice of action on a any claim for refund of tax or interest within six months after the claim is filed, the taxpayer, prior to mailing of notice of action on the refund claim, may consider the claim disallowed. The taxpayer may appeal to the department for a hearing pursuant to § 42-122.

Ariz. Rev. Stat. Ann. § 42-134 (Supp. 1992):

Interest

A. If it is provided by law that interest applies as determined pursuant to this section, the department shall appy the rate of interest, compounded annually,

established by the director in the same manner and at the same times as prescribed by § 6621 of the United States internal revenue code. On January 1 of each year the department shall add any interest outstanding as of that date to the principal amount of the tax. For purposes of this section the amount added to the principal is thereafter considered a part of the principal amount of the tax and accrues interest pursuant to this section.

B. If the tax, whether determined by the department or the taxpayer, or any portion of the tax is not paid on or before the date prescribed for its payment the department shall collect, as a part of the tax, interest on the unpaid amount at the rate determined pursuant to this section from the date prescribed for its payment until it is paid.

Ariz. Rev. Stat. Ann. § 42-136 (Supp. 1992):

Civil penalties; definition

A. If a taxpayer fails to make and file a return for a tax administered pursuant to this article on or before the due date of the return or the due date as extended by the department, then, unless it is shown that the failure is due to reasonable cause and not due to wilful neglect, five per cent of the tax found to be remaining due shall be added to the tax for each month or fraction of a month elapsing between the due date of the return and the date on which it is filed. . . .

* * * *

D. A person who fails to pay the tax within the time prescribed shall pay a penalty of ten per cent in addition to the tax, unless it is shown that the failure is due to reasonable cause and not due to wilful neglect. . . .

E. In the case of a deficiency, for which a determination is made of an additional amount due, which is due to negligence but without intent to de-

fraud, the person shall pay a penalty of ten per cent of the amount of deficiency.

F. If part of a deficiency is due to fraud with intent to evade tax, fifty per cent of the total amount of the tax, in addition to the deficiency, interest and other penalties provided in this section, shall be assessed, collected and paid as if it were a deficiency.

* * * *

H. A person who, with or without intent to evade any requirement of this article or any lawful administrative rule of the department under this article, fails to file a return or to supply information required under this article or who, with or without such intent, makes, prepares, renders, signs or verifies a false or fraudulent return or statement or supplies false or fraudulent information shall pay a penalty of not more than one thousand dollars. . . .

I. If the taxpayer files what purports to be a return of any tax administered pursuant to this article but which is frivolous or which is made with the intent to delay or impede the administration of the tax laws, that person shall pay a penalty of five hundred dollars.

Ariz. Rev. Stat. Ann. § 42-137 (1991):

Criminal violations; classifications; place of trial; definition

* * * *

B. It is a class 5 felony to:

1. Knowingly fail to pay any tax administered pursuant to this article due or believed due by the taxpayer with intent to evade the tax.

Ariz. Rev. Stat. Ann. § 43-1001 (1980):

Definitions

In this chapter, unless the context otherwise requires:

1. "Arizona adjusted gross income" of a resident individual means his Arizona gross income subject to modifications specified in §§ 43-1021 and 43-1022.

2. "Arizona gross income" of a resident individual means his federal adjusted gross income for the taxable year, computed pursuant to the Internal Revenue Code.

Ariz. Rev. Stat. Ann. § 43-1022 (1980) (current version at § 43-1022 (Supp. 1992)):

Subtractions from Arizona gross income

In computing Arizona adjusted gross income, the following amounts shall be subtracted from Arizona gross income:

* * * *

3. Benefits, annuities and pensions received from the state retirement system, the state retirement plan, the judges' retirement fund, the public safety personnel retirement system or a county or city retirement plan.

4. Income received as annuities under the United States civil service retirement system from the United States government service retirement and disability fund, in an amount not to exceed two thousand five hundred dollars.

Ariz. Code Ann. § 73-1544(e) (1939) (repealed)

(e) If the commission shall fail or neglect to act on any claim for refund or credit within one [1] year after the receipt thereof, such neglect shall have the effect of allowing such claim and the commission shall certify such refund or credit.

III. RELEVANT PORTIONS OF THE ARIZONA REGULATIONS

Ariz. Admin. Comp. R15-2-601 through R15-2-645 (Supp. 92-1), Arizona Department of Revenue:

Article 6. ABATEMENTS, CREDITS AND REFUNDS

REFUNDS

R15-2-601. Reserved
R15-2-602. Reserved
R15-2-603. Reserved
R15-2-604. Reserved
R15-2-605. Reserved
R15-2-606. Reserved
R15-2-607. Reserved
R15-2-608. Reserved
R15-2-609. Reserved
R15-2-610. Reserved
R15-2-611. Reserved
R15-2-612. Reserved

INTEREST ON REFUNDS

R15-2-621. Reserved
R15-2-622. Reserved
R15-2-623. Reserved
R15-2-624. Reserved
R15-2-625. Reserved
R15-2-626. Reserved

OTHER TAX ABATEMENTS

R15-2-641. Reserved
R15-2-642. Reserved
R15-2-643. Reserved
R15-2-644. Repealed
R15-2-645. Repealed

Ariz. Admin. Comp. R15-10-101 (Supp. 81-3), Arizona Department of Revenue, Hearing Procedures:

> Purpose
>
> The law establishes that the Department of Revenue (Department) shall provide an effective opportunity for taxpayers to petition for hearing, correction or redetermination of proposed tax assessments issued by the Tax Division (Division). These Rules are hereby promulgated by the Department to inform each taxpayer of the procedures he or she should follow in filing petitions for hearing, correction or redetermination of a proposed tax assessment.

Ariz. Admin. Comp. R15-10-120 (Supp. 86-4), Arizona Department of Revenue, Hearing Procedures:

> Review or determination of decision of Hearing Officer
>
> A. The decision of the Hearing Officer is the final decision of the Department unless within fifteen (15) days of the receipt of the Hearing Officer's decision by the taxpayer, the taxpayer or the Division petitions the Director of the Department for a review, or unless the Director, acting upon his own motion. . . determines need for review of the Hearing Officer's decision.
>
> B. Grounds for reversal may include the following:
>
> * * * *
>
> 7. That the decision, findings of fact, or conclusions of law is not justified by the evidence or is contrary to law.
>
> C. On petition for review, or upon his own motion, the Director of the Department may open the decision of the Hearing Officer, take additional evidence, amend findings of fact and conclusions of law or make new findings and conclusions, and issue a new decision. . . .

Ariz. Admin. Comp. R16-3-112 (Supp. 80-6), State Board of Tax Appeals:

> Place of hearing; time allowed
>
> Oral hearings are held in the Board's hearing room in Phoenix, Arizona. Hearings shall ordinarily be conducted between the hours of 9 A.M. and 5 P.M. and are scheduled to last for not more than one hour. If additional time is needed, this may be arranged in advance through the Clerk of the Board.
>
> . . .

APPENDIX K

NOTICE TO FEDERAL RETIREES

As of September 15, 1989, a lawsuit concerning the taxability of federal retirement benefits is pending in the court system. This lawsuit will determine whether or not the state must refund any taxes paid on these benefits in past years. The statute of limitations for income tax refunds is four years. If you paid Arizona income tax on federal retirement benefits for tax year 1985, you can protect your claim for a possible refund by mailing the notice below on or before April 16, 1990. In addition, you will stop the running of a statute of limitation for all other applicable years by filing this notice. If refunds are due upon final resolution of the lawsuit, additional financial information may be required to determine the proper amount.

NOTICE OF CLAIM

I hereby claim a refund of any Arizona income tax paid in 1985, 1986, 1987 and 1988 on federal retirement benefits.

NAME _____

SOC. SEC. NO. _____

MAILING ADDRESS _____

_____

SIGNATURE _____ DATE _____

MAIL NOTICE TO:

ARIZONA DEPARTMENT OF REVENUE
1600 WEST MONROE
PHOENIX, ARIZONA 85007
ATTN: PROTECTIVE CLAIMS

APPENDIX L

IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

---

1 CA-CIV 4250
MARICOPA County Superior Court No. C 350648

VALLEY VENDORS CORPORATION,
an Arizona corporation,
Appellant,

vs.

CITY OF PHOENIX,
a municipal corporation,
Appellee.

APPELLANT'S REPLY BRIEF

TAYLOR & PETICA, P.C.

By RON PETICA
7505 East Angus Drive
Scottsdale, Arizona 85251
Attorneys for Appellant

* * * *

IV. *Declaratory Relief is Available*

City of Phoenix v. Phoenix Newspapers, Inc., 100 Az 189, 412 P2d 692, contra to Appellee's assertion, did *not* involve a decision that even though the taxpayer raised unconstitutional discrimination, the Court upheld payment under protest provisions—although discrimination was *raised* by the taxpayer, the Court *specifically* did not decide the case on this issue (412 P2d at 696).

City of Phoenix vs. Ariz. Sash, Door and Glass Co., 80 Az 100, 293 P2d 438, did *not* raise the constitutionality of any particular assessment, nor did it address itself to administrative remedies granted by the tax ordinance.

Again, Appellant is not alleging that the Phoenix Privilege License Tax Ordinance is invalid (except for the administrative deficiencies); only (in the Complaint) that the City officials are acting arbitrarily and illegally against Appellant in its assessments against Appellant.

* * * *

APPENDIX M

STATE OF ARIZONA
BUDGET REQUEST

TRANSMITTAL STATEMENT

		FY 1994	FY 1995
State Board of Tax Appeals	Total Amount Requested	$772,200	$722,200
Arizona Revised Statutes 42-171	General Fund	$772,200	$722,200
	Other Appropriated Funds	———	———
	Federal Funds	———	———
	Other Non-Appropriated Funds	———	———

GOVERNOR SYMINGTON:

This and the accompanying budget schedules, statements, and explanatory information constitute the operating budget estimates of this agency for proposed expenditures for the 1994 and 1995 fiscal years in accordance with A.R.S. 35-113.

All statements and explanations contained in the estimates submitted are true and correct to the best of my knowledge.

Agency Head RUBEN M. MEDINA

Title CLERK OF THE BOARD

Signature /s/ Ruben M. Medina

Request Prepared by RUBEN M. MEDINA
AND PHILLIP G. VIATOR

Phone 542-3288
AND 542-7070

Date Prepared 17-Sep-92

Transmittal Statement

Agency Name and Number State Board of Tax Appeals—0188
Program Name and Number Division Two—5610
Fund Name and Number General Fund—9001

SCHEDULE 4
SERVICE MEASUREMENTS

Service Measurements Income, Sales, Use, A.R.S. 42-171	Actual FY 1990	Actual FY 1991	Actual FY 1992	Estimated FY 1993	Estimated FY 1994 (with Dec. Pkg.)	Estimated FY 1995 (with Dec. Pkg).
Tax Appeals Pending From Previous Year:						
- Income-Corporation/Individual	21	20	45	57	86	120
- Sales/Use	42	53	77	89	110	140
- Other	1	1	5	5	10	26
Total Appeals Pending	64	74	127	151	206	286
Tax Appeals Filed During Year:						
- Income-Corporation/Individual	33	43	62	70	80	90
- Sales/Use	52	86	61	80	90	110
- Other	0	9	16	20	25	35
	85	138	139	170	195	235
Total Appeal Caseload	149	212	266	321	401	521
Amounts Involved (Excludes Interest to Date Of Payment)	$13.3 Million	$27.0 Million	$47.5 Million	$51.0 Million	$64.2 Million	$83.4 Million
Average Amount Per Appeal (Excludes Interest)	$89,300	$127,300	$178,600	$160,000	$160,000	$160,000
Number of Cases Decided/Resolved During Year	75	85	115	115	115	115
Amounts Involved In Cases Decided	$6.5 Million	$7.1 Million	$19.5 Million	$18.4 Million	$18.4 Million	$18.4 Million
Tax Appeals Carried Over To Following Year	74	127	151	206	286	406
Amounts Involved On Carried Over Appeals (Excludes Interest)	$6.8 Million	$19.9 Million	$28.0 Million	$33.0 Million	$45.8 Million	$65.0 Million
* * * * *						
Number Of Copies Reproduced	64,200	76,600	85,200	95,000	140,000	190,000
Total Board Business Days	168	187	220	220	220	220

Date Prepared 18-Sep-92

APPENDIX N

PUBLIC SALARY TAX ACT OF 1939

AN ACT

Relating to the taxation of the compensation of public officers and employees.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Public Salary Tax Act of 1939".

TITLE I

SECTION 1. Section 22(a) of the Internal Revenue Code (relating to the definition of "gross income") is amended by inserting after the words "compensation for personal service" the following: ("including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing)".

SEC. 2. Section 116(b) of the Internal Revenue Code (exempting compensation of teachers in Alaska and Hawaii from income tax) is repealed.

SEC. 3. Section 22(a) of the Internal Revenue Code is amended by adding at the end thereof a new sentence to read as follows: 'In the case of judges of courts of the United States who took office on or before June 6, 1932, the compensation received as such shall be included in gross income".

SEC. 4. The United States hereby consents to the taxation of compensation, received after December 31, 1938, for personal service as an officer or employee of the United States, any Territory or possession of political subdivision thereof, the District of Columbia, or any agency

or instrumentality of any one or more of the foregoing, by any duly constituted taxing authority having jurisdiction to tax such compensation, if such taxation does not discriminate against such officer or employee because of the source of such compensation.

TITLE II

SEC. 201. Any amount of income tax (including interest, additions-to-tax, and additional amounts) for any taxable year beginning prior to January 1, 1938, to the extent attributable to compensation for personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing—

(a) shall not be assessed, and no proceeding in court for the collection thereof shall be begun or prosecuted (unless pursuant to an assessment made prior to January 1, 1939);

(b) if assessed after December 31, 1938, the assessment shall be abated, and any amount collected in pursuance of such assessment shall be credited or refunded in the same manner as in the case of an income tax erroneously collected; and

(c) shall, if collected on or before the date of the enactment of this Act, be credited or refunded in the same manner as in the case of an income tax erroneously collected, in the following cases—

(1) Where a claim for refund of such amount was filed before January 19, 1939, and was not disallowed on or before the date of the enactment of this Act;

(2) Where such claim was so filed but has been disallowed and the time for beginning suit with respect thereto has not expired on the date of the enactment of this Act;

(3) Where a suit for recovery of such amount is pending on the date of the enactment of this Act; and

(4) Where a petition to the Board of Tax Appeals has filed with respect to such amount and the Board's decision has not become final before the date of the enactment of this Act.

SEC. 202. In the case of any taxable year beginning after December 31, 1937, and before January 1, 1939, compensation for personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing, shall not be included in the gross income of any individual under Title I of the Revenue Act of 1938 and shall be exempt from taxation under such title, if such individual either—

(a) did not include in his return for a taxable year beginning after December 31, 1936, and before January 1, 1938, any amount as compensation for personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing; or

(b) did include any such amount in such return, but is entitled under section 201 of this Act to have the tax attributable thereto credited or refunded.

SEC. 203. Any amount of income tax (including interest, additions to tax, and additional amounts) collected on, before, or after the date of the enactment of this Act for any taxable year beginning prior to January 1, 1939, to the extent attributable to compensation for personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing, shall be credited or refunded in the same manner as in the case of an income tax erroneously collected, if claim for refund with respect thereto is filed after January 18, 1939, and

the Commissioner of Internal Revenue, under regulations prescribed by him with the approval of the Secretary of the Treasury, finds that disallowance of such claim would result in the application of the doctrines in the cases of Helvering against Therrell (303 U.S. 218), Helvering against Gerhardt (304 U.S. 405), and Graves et al. against New York ex rel O'Keefe, decided March 27, 1939, extending the classes of officers and employees subject to Federal taxation.

SEC. 204. Neither section 201 nor section 203 shall apply in any case where the claim for refund, or the institution of the suit, or the filing of the petition with the Board was, at the time filed or begun, barred by the statute of limitations properly applicable thereto.

SEC. 205. Compensation shall not be considered as compensation within the meaning of sections 201, 202, and 203 to the extent that it is paid directly or indirectly by the United States or any agency or instrumentality thereof.

SEC. 206. The terms used in this Act shall have the same meaning as when used in Chapter 1 of the Internal Revenue Code.

SEC. 207. No collection of any tax (including interest, additions to tax, and penalties) imposed by any State, Territory, possession, or local taxing authority on the compensation, received before January 1, 1939, for personal service as an officer or employee of the United States or any agency or instrumentality thereof which is exempt from Federal income taxation and, if a corporate agency or instrumentality, is one (a) a majority of the stock or which is owned by or on behalf of the United States, or (b) the power to appoint or select a majority of the board of directors of which is exercisable by or on behalf of the United States, shall be made after the date of the enactment of this Act.

SEC. 208. This title shall not apply with respect to any officer or employee of a State, or any political subdivision

thereof, or any agency or instrumentality of any one or more of the foregoing, after the Secretary of the Treasury has determined and proclaimed that it is the policy of such State to collect from any individual any tax, interest, additions to tax, or penalties, on account of compensation received by such individual prior to January 1, 1939, for personal service as an officer or employee of the United States or any agency or instrumentality thereof. In making such determination the Secretary of the Treasury shall disregard the taxation of officers and employees of any corporate agency or instrumentality which is not exempt from Federal income taxation, or which if so exempt is one (a) a majority of the stock of which is not owned by or on behalf of the United States and (b) the power to appoint or select a majority of the board of directors of which is not exercisable by or on behalf of the United States.

SEC. 209. In the case of the judges of the Supreme Court, and of the inferior courts of the United States created under article III of the Constitution, who took office on or before June 6, 1932, the compensation received as such shall not be subject to income tax under the Revenue Act of 1938 or any prior revenue Act.

SEC. 210. For the purposes of this Act, the term "officer or employee" includes a member of a legislative body and a judge or officer of a court.

SEC. 211. If either title of this Act, or the application thereof to any person or circumstances, is held invalid, the other title of the Act shall not be affected thereby.

Approved, April 12, 1939.

APPENDIX O

Excerpts from Arizona's Uniform Declaratory Judgments Act

Ariz. Rev. Stat. Ann. § 12-1831 (1982):

Scope

Courts of record within their respective jurisdictions shall have power to declare rights, status, and other legal relations whether or not further relief is or could be claimed. No action or proceeding shall be open to objection on the ground that a declaratory judgment or decree is prayed for. The declaration may be either affirmative or negative in form and effect, and such declarations shall have the force and effect of a final judgment or decree.

Ariz. Rev. Stat. Ann. § 12-1832 (1982):

Power to construe, etc.

Any person . . . whose rights, status or other legal relations are affected by a statute . . . may have determined any question of construction or validity arising under the . . . statute . . . and obtain a declaration of rights, status or other legal relations thereunder.

Ariz. Rev. Stat. Ann. § 12-1835 (1982):

Enumeration not exclusive

The enumeration in §§ 12-1832, 12-1833 and 12-1834 does not limit or restrict the exercise of the general powers conferred in § 12-1831, in any proceeding where declaratory relief is sought, in which a judgment or decree will terminate the controversy or remove an uncertainty.

Ariz. Rev. Stat. Ann. § 12-1838 (1982):

Supplemental relief

Further relief based upon a declaratory judgment or decree may be granted whenever necessary or proper. . . .

Ariz. Rev. Stat. Ann. § 12-1842 (1982):

Construction

This article is declared to be remedial; its purpose is to settle and to afford relief from uncertainty with respect to rights, status and other legal relations; and it is to be liberally construed and administered.